Nestor Healthcare Group plc

Annual Report and Accounts 2004

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Contents

Chairman's Statement

2004 has been a year of significant challenge for Nestor with two of the Group's three markets undergoing unprecedented degrees of change. Healthcare Staffing volumes have been adversely impacted by the extension of NHS Professionals at the same time as prices and margins have been lowered through the negotiation of NHS framework agreements. In Primary Care the previous GP customer base has been largely replaced as the responsibility for the provision of out-of-hours services has been transferred to Primary Care Trusts (PCTs).

Management, under the leadership of Stephen Booty, has responded robustly, but responsibly, in implementing a restructuring and cost reduction programme designed to ensure the revised needs of customers are met in a cost effective, professional manner. The extent of the reorganisation is described in detail below. This programme has been successfully implemented and will benefit ongoing earnings.

The results for 2004 reflect these difficult market conditions and contain a number of exceptional items, which recognise the actions taken to reorganise and rationalise the Group's cost base, as well as a substantial write-down in the goodwill arising from the acquisition in 2001 of Healthcall. The benefits of the reorganisation have already started to be realised with improved profit performance across our businesses in the second half of 2004.

Results summary

	2004	2003
Statutory results		
Turnover	£389.8m	£423.2m
(Loss)/Profit before tax	£(55.6m)	£13.6m
(Loss)/Earnings per share	(66.4p)	10.5p
Business performance		
Operating profit	£20.6m	£28.8m
Interest	£(5.4m)	(£4.1m)
Profit before tax	£15.2m	£24.7m
Earnings per share	12.0p	23.2p

Statutory results are stated after goodwill amortisation and exceptional charges of £8.8m (2003: £8.4m) and £62.0m (2003: £2.7m) respectively. Business performance results, which are used throughout this statement, the Chief Executive's Review and the Financial Review, exclude goodwill amortisation and exceptional charges and reflect the manner in which the business is managed and its underlying operating performance.

Business performance profit before tax for the year ended 31st December 2004 was £15.2m and was in line with our expectations. This includes a continuing strong performance in Social Care where the Group has invested significant funds and resources in the last two years. As predicted Primary Care, after suffering a loss in the first half of the year has achieved a profit in the second half and the performance of Healthcare Staffing has stabilised, generating a net margin of 4.9%. The results of the three business areas are discussed in more detail in the Chief Executive's review.

Business reorganisation and Exceptional Items

Business units are now organised and managed according to the markets they serve, namely Healthcare Staffing, Social Care and Primary Care, with their respective customer bases being NHS Acute Trusts, Local Authorities and Primary Care Trusts. These operations are now supported by a single set of specialist support functions.

The reduction in demand for our services has led to a rationalisation of the branch network in both Healthcare Staffing and Primary Care. Within Healthcare Staffing a total of 33 branches have been closed or merged leaving 86 operating locations. Primecare's original network of 29 branches has been rationalised to 10 as the trend of PCTs choosing an NHS-based solution for out-of-hours provision became apparent. In addition Primecare's Clinical Response Centre (CRC) in Sheffield closed at the end of November with the ongoing call handling demand being managed by

Management has responded robustly, but responsibly, in implementing a restructuring and cost reduction programme designed to ensure the revised needs of customers are met in a cost effective, professional manner.

regional offices, supported by the remaining CRC in Birmingham.
The majority of the value of Exceptional Items was included in the Interim accounts, but it was noted at the time that further charges would be made in the second half of the year in line with Financial Reporting Standards. The total of £62.0m charged as Exceptional Items for the year is analysed in the Financial Review.

Cash flow and borrowings
Closing net borrowings were £84.6m (year-end 2003: £89.3m), comfortably within the Group's facilities. Cash flow from operations totalled £29.6m (2003: £25.0m) as tight controls on working capital were maintained.

Acquisitions
The extension of our network of social care providers remains central to the strategic development of the Group. Despite our focus on the business reorganisation during the year, we completed five acquisitions at a cost of £2.5m, with a further £0.2m potentially payable, subject to performance. In addition, a further £2.1m was paid as deferred consideration in respect of acquisitions made in 2003.
In January 2005, the Group completed the acquisition of eight social care branches from Community Careline Services Limited at a cost of £1.6m, with potential additional deferred consideration of £0.2m.

Earnings per share
Business performance earnings per share of 12.0p compares to 23.2p in 2003. The underlying tax rate on trading profit is 30%, compared to 18% in the previous year when the Group benefited from the tax efficient reorganisation of its legal structure, which commenced in 2002. This benefit ceased in June 2003.

Dividends
The Board is recommending a final dividend per share of 1.50p, having not proposed a dividend at the interim stage. The total dividend per share paid for the year ended 31st December 2003 was 9.62p.

Board changes
The appointment, in January 2004, of Sir Andrew Foster and Roger Dye as Independent Non-Executive Directors, was noted in the Chairman's statement in last year's report.

Justin Jewitt stood down as Chief Executive of Nestor in May 2004. Stephen Page, previously Managing Director of the Services Division, left the Group in August with the ending of the two-division structure. The Board thanks both Justin and Stephen for their contribution to Nestor in their time with the Group.

Stephen Booty, previously Managing Director of the Personnel Division, was appointed Chief Executive in December 2004, having taken over as Acting Chief Executive in May. Stephen's expertise in business processes and cost management is already serving the Group well as the reorganisation and restructuring strategy is implemented.

The reduced number of Board members has improved focus and direction whilst, through a strong team of non-executive directors, retaining a robust approach to corporate governance.

Staff
Nestor is an organisation charged with the provision of the highest standards of care towards patients and clients and depends upon its employees and members for its delivery. The scale of change and disruption incurred in 2004 with the business reorganisation is evident in the reduction in average employee numbers from 4,800 to 3,700. Throughout this period Nestor employees and members have maintained the highest standards of professionalism and care and the Board thanks them all for their continuing dedication and enthusiasm.

Outlook
The reorganisation of business operations is now substantially complete but management will continue to seek ways to further rationalise the cost base as short-term improvements in market conditions are not considered likely. The actions taken in the second half of 2004 have stabilised the Group's financial performance and the revised structure will ensure a more focused approach as the effects of structural changes in our Primary Care and Healthcare Staffing markets become more evident.

John Rennocks, Chairman
7th March 2005

Chief Executive's Review

Business units are now organised and managed according to the markets they serve, namely, Healthcare Staffing, Social Care and Primary Care, with their respective major customer bases being NHS Acute Trusts, Local Authorities and Primary Care Trusts.

Our internal financial reporting mirrors the operational structure as does the presentation below. The additional segmentation splits the business reported in previous years as 'Personnel Division' between Healthcare Staffing and Social Care. Each of the individual branches, many of which have covered all areas of healthcare staffing provision and the more complex domiciliary care services, have now been segregated and dedicated specifically to either Healthcare Staffing or Social Care. The requirements of the "customers" in these markets are quite different and need different skills and infrastructures. Most often a "staffing" requirement is for a specific type of clinician, at short notice, often on the same day and for a short period of time. A social care opportunity usually involves a thorough needs assessment leading to a specific care package for an individual, which could be provided over a lengthy period of time.

Financial Performance

	2004 Turnover	2004 Operating profit	2003 Turnover	2003 Operating profit
Healthcare Staffing	£166.0m	£8.1m	£210.0m	£18.6m
Social Care	£103.5m	£12.7m	£89.3m	£10.0m
Primary Care	£120.3m	£(0.2m)	£123.9m	£0.2m
Total	£389.8m	£20.6m	£423.2m	£28.8m

Healthcare Staffing

Our Healthcare Staffing businesses provide temporary, locum or permanent staffing solutions to the healthcare market, including NHS trusts, PCTs, private hospitals, nursing and residential homes and industry. Nurses, according to their grade and specialism, are provided through the BNA, Grosvenor and Mayfair brands. The three brands are well recognised for general, mental health, and specialist nursing respectively but are increasingly working together to present a Nestor "one stop shop" solution for staffing requirements. This approach is increasingly popular with the larger acute trusts and with PCTs. Doctors and allied healthcare professionals are supplied through the Medic International, Holt, Cornelle and Pinnacle businesses.

The impact on volume of NHS Professionals (NHSP), combined with the pricing pressure from the extension of NHS regional framework agreements, is evident in the turnover reduction of 21% and the operating margin achieved of 4.9%, compared to last year's 8.9%. As all but two of the major nursing bank contracts have now transferred to NHSP, the volume of hours sold to the NHS is expected to stabilise at the current level.

Nestor's nurse agency and medical services businesses are all approved suppliers under the NHS framework agreements and additionally are often first call providers to NHSP for shifts they are unable to fill. Frameworks are in place throughout England for the supply of nurses, doctors and allied healthcare professionals. The pricing under the current frameworks under-pin the margin

earned in Healthcare Staffing, which is expected to be maintained at the current level. All of the NHS framework agreements encompass rigorous recruitment and quality requirements, which has involved ongoing investment. We have also experienced a reduction in the number of professionals who supplement their substantive NHS roles with temporary assignments, as these recruitment and quality requirements are more rigorous via an agency, than those applied in their roles within the NHS.

Over and above the rigorous NHS framework requirements, nurse agencies are regulated and monitored by the Commission for Social Care Inspection (CSCI). These regulations include criminal record checks, health checks and right to work verification. CSCI also regulates and monitors our Social Care businesses. The nurse agency and social care businesses are all able to comply with this regulation.

The overall reduction in demand for our services has led to a rationalisation of the branch network. A total of 33 branches have been closed or merged leaving 86 operating locations. This still represents comprehensive national coverage and remains the most extensive network of dedicated healthcare branches maintained by any provider.

The volume of NHS work has now stabilised. The lower levels of NHS work along with the new dedicated focus have motivated the regeneration of our non-NHS customer base. Previously with the volume of business available on a regular basis through the NHS, other market opportunities had not been effectively pursued. Private Hospitals, Nursing Homes, Care Homes, Community Healthcare, Prisons and Industry all offer opportunities for flexible, cost effective staffing solutions, as indeed do the recent privately managed "treatment centres" especially with the requirements for "staffing additionality".

Social Care

These business units provide managed services in the community to support the quality of life for those individuals in need of personal care, primarily in their own homes. Services are commissioned by local authorities and PCTs, or purchased by a private individual.

Social Care margin remains strong at over 12% augmented by volume increases from acquisitions made in 2003, together with a further five acquisitions completed in 2004 and the development of new territories. The separation of our social care businesses from the previous BNA and Grosvenor groupings has created a dedicated approach to social care, operating from 117 locations. In addition our franchise business, Carewatch, which is wholly dedicated to domiciliary care, operates from a further 130 locations, making Nestor the largest provider in what remains a very fragmented sector. The acquisitions completed in 2003 and 2004 continue to generate excellent returns. The success of the acquisition programme was one of the factors which led to the change in structure and the de-merging of the Goldsborough business from BNA. After its acquisition in 2001, Goldsborough was absorbed into BNA in order to achieve a rationalisation of back office systems, which was implemented successfully. However, as our acquisitions have demonstrated, the approach to social care, with the prospect of long-term individually designed care packages, requires dedicated attention and the cultivation of close working relationships with local authorities and the various local government agencies responsible for ensuring care in the community. Nestor businesses, whilst focused on the delivery of a local service, also benefit from the support of Group technology and clinical governance systems.

Social services continue to extend the outsourcing of care work to the independent sector and opportunities for organic growth remain in elder care as well as areas such as dementia, extra care housing support, direct payments, learning disability and palliative care.

The priority for Nestor is to maintain a high standard of service, including clinical governance, to all our customers.

These opportunities are being investigated in order to broaden our service offering and better define our acquisition targets. An example of a more specialist provider is New Horizons, acquired in late 2003, which focuses exclusively on learning disability. Nevertheless the social care environment is becoming more sophisticated and challenging, as regulation from the CSCI is implemented across England and Wales, with the equivalent through the Scottish Care Commission. With the standards comes the requirement, by April 2008, for 50% of all care delivered to be provided by careworkers trained to NVQ 2 levels; this is an important investment. Indeed, one of the critical success factors for our business is the ability to recruit and retain suitable careworkers in every locality. To effectively develop this opportunity the Group acquired Suffolk NVQ consortium, a specialist NVQ training company at the end of 2003.

The Government continues to invest within the domiciliary care sector, yet this is not always reflected in improved charge rates and members pay, given the investment required in regulatory compliance and careworker training. The intended introduction of a system of direct payments will enable local councils to provide funds to service users to purchase their care from individuals as well as independent suppliers. This will require careful monitoring as it could lead to the introduction of an unregulated work force into the market. The priority for Nestor is to maintain a high standard of service, including clinical governance, to all our customers, whilst offering attractive conditions of work for the careworkers who deliver the care.

Primary Care

Primary Care comprises three main business units. Primecare Primary Care provides out-of-hours services to GPs and Primary Care Trusts (PCTs); Forensic Medical delivers care in secure environments and to Police Authorities and Nestor Disability Analysis (NDA) provides screening services for the Benefits Agency.

As forecast Primary Care, having suffered a loss in the first half of 2004, has been profitable in the second half and is expected to continue to improve. This progress has been achieved by rationalising the cost base of Primecare Primary Care in line with the reduction in volume, whilst the other business units have continued to perform satisfactorily.

In the Primecare Primary Care business the transfer of contracts to PCTs is largely complete. The ongoing business is contracted with 45 PCTs with the major concentrations being in the North East, the Midlands and South Wales. Turnover in 2005, being a full year on the reduced contract bank, is anticipated to be approximately £40m compared to £72m in 2004. Over the critical Christmas and New Year period, Primecare's operations were robust and delivered a high standard of service. It is evident that a number of the new service providers struggled with the volumes to be handled at peak times and, since the beginning of the new year, Primecare has had renewed interest from a number of PCTs. With the collapse of the North Yorkshire doctors' cooperative solution, Primecare has recently been appointed to operate the service for Scarborough PCT.

The operational structure of the business has been reorganised with the establishment of smaller scale local call centres supported by the Birmingham CRC, which provides an effective back-up to the local centres as well as retaining the capacity to increase the level of call handling.

Forensic Medical continued to perform well in 2004 on turnover up 4% on the previous year at £16.7m. The year finished well with the business being awarded the contract to support Leicestershire Police following the winning of the Nottinghamshire contract and the renewal of West Midlands. There is a distinct trend amongst Police Authorities to more actively consider the use of private providers for their medical services. Primecare FMS has been proactive in the introduction of more nursing resource in support of doctors to provide a more flexible and cost-effective service and the prospects are good for more contract wins in 2005.

NDA continues to support Atos Origin through the provision of sessional doctors to carry out disability assessments. Turnover of £26m produced a profit of £0.6m. The current contract expires at the end of August 2005. NDA will take on an enhanced role in the provision of the service in the event that Atos Origin is successful in retaining the contract.

Looking ahead, the Primary Care business will be managed in a more cohesive way, with Primecare Primary Care and the Forensic Medical businesses being merged into a single entity. This will enable a further streamlining of the cost base and reporting structure but, more particularly, will better optimise the use of our pool of doctor and nurse resource.

Stephen Booty, Chief Executive
7th March 2005

Financial Review

With the reorganisation of the business the segmental analysis of performance has been changed from the previous two-division structure of 'Personnel' and 'Services' to the three business streams of 'Healthcare Staffing', 'Social Care' and 'Primary Care'. Comparative figures for the previous year have been amended accordingly.

Turnover

Turnover for the Group reduced by 7.9% to £389.8m (2003: £423.2m).

Whilst turnover in Social Care continued to grow with the benefit of acquisitions, Healthcare Staffing saw a decline of 21% with the combined impact of the volume transferred to NHS Professionals and the pressure on pricing exerted through the framework agreements. Primary Care turnover was steady but will reduce in 2005 as PCTs take on the provision of out-of-hours services.

Operating profit and margins

The Group's operating profit, before goodwill amortisation and exceptional items, reduced by 28.5% to £20.6m (2003: £28.8m), representing an operating profit margin (before goodwill amortisation and exceptional items) of 5.3% (2003: 6.8%).

Healthcare Staffing's operating profit, (before goodwill amortisation and exceptional items) was affected by the issues mentioned above with margin reduced to 4.9% from 8.9% last year. As all but two of the main bank contracts have now been taken over by NHSP, the margin is not expected to decline any further.

Social Care maintained a strong margin performance at 12.3% (2003: 11.2%). This included a full year contribution from businesses acquired in 2003 and the part-year benefit of acquisitions made in 2004.

Primary Care recorded an operating loss of £0.2m (2003 profit: £0.2m) for the year but achieved an operating profit of £1.5m in the second half as Primecare Primary Care's cost base was reduced in line with the shrinkage in volume.

Exceptional items

The nature and extent of the costs and accounting provisions associated with the goodwill impairment and the fundamental business reorganisation are such that, under Financial Reporting Standard FRS3, they are separately disclosed from the underlying trading result as 'Exceptional Items'.

The total of £62.0m charged as 'Exceptional Items' for the year is analysed as follows:

Goodwill impairment	£48.6m
Property provisions	£4.9m
Asset impairments	£4.8m
Severance and other reorganisation costs	£2.1m
Settlement of US tax liability	£1.6m

The goodwill impairment relates to the carrying value of goodwill arising from the purchase of Healthcall in 2001. With the changing shape of the Primary Care market and the intention of many PCTs to adopt an in-house solution to the provision of out-of-hours services, the medium term prospects for Primecare Primary Care have declined. Management has undertaken a detailed re-forecasting exercise for the business, the discounted cash flows of which form the basis of the goodwill valuation. The result of this exercise, using the Group's cost of capital, reduces the carrying value of the Healthcall goodwill to £33.0m at the year-end and causes the exceptional charge of £48.6m.

The property provisions are the result of a detailed review of the Group's property

portfolio to identify any onerous leases following the rationalisation of the branch network across all our business activities, the closure of the Sheffield Clinical Response Centre (CRC) and the restructuring of head office. The provision estimates the length of time properties will be vacant, together with any dilapidation costs and other costs associated with the termination or disposal of leases.

Asset impairments relate to the closure of the same properties referred to above and are primarily the write-off of infrastructure and fixtures and fittings, which cannot be used elsewhere. The major element included in the £4.8m charge is the write down of £3.4m in the assets of the Sheffield CRC, which closed at the end of November 2004.

Other reorganisation costs relate largely to severance costs paid or payable to employees whose redundancies had been initiated by the end of the year. The US tax liability relates back to the sale of the Group's American staffing business, Cross Country Staffing (CCS) in 1999. This issue had been disclosed as a Contingent Liability in Nestor's accounts since 1999 and relates to the earlier provision of travel benefits to nurses, which were paid with no provision for deduction of payroll tax. The Internal Revenue Service of the US (the IRS) had issued a payroll tax assessment in 1998 against CCS and its US partners to a value of US$21.8 million. Nestor's share of the liability, given the dates involved and the shared ownership of the business concerned, equates to 22% of the overall liability. Attempts to settle the case have been ongoing and, on 17th February 2004, CCS and its US partners submitted a written offer to the US Department of Justice, containing their proposal to settle all claims for a cash sum of US$13.0 million, the Group's share of which would be US$2.9 million. The Group has now received advice that the US authorities are minded to accept the settlement terms so offered. It is expected therefore that the settlement, plus costs, will be confirmed and paid during 2005.

Goodwill

At 31st December 2004, following the exceptional impairment described above in connection with the Healthcall acquisition, goodwill on the balance sheet amounted to £106.8m (2003: £161.1m). From 2005 onwards, following adoption of International Financial Reporting Standards, there will be no ongoing amortisation of goodwill, but a reassessment at the end of every reporting period to assess whether the value of any goodwill retained in the balance sheet should be written down according to the future values forecast to be earned from that goodwill.

Pre-tax profit

Profit before tax, exceptional items and goodwill amortisation amounted to £15.2m (2003: £24.7m), a reduction of 38.5%.

Taxation

The tax charge for the year was £2.4m (2002: £4.4m). The average tax rate on profit, before goodwill amortisation and exceptional items, was 30% (2003: 18%). The lower average tax rate in 2003 arose from two tax credits, being £1.7m relating to a reclaim of tax relating to under-let properties and a further £1.5m in respect of tax relief claimable on the amortisation of goodwill. Excluding these items the normalised rate was 30%, consistent with 2004.

Earnings per share

The basic adjusted earnings per share, before exceptional items and goodwill amortisation, were 12.0p (2003: 23.2p) a reduction of 48.3%. This reflects the reduction in pre-tax profit and the increased average tax rate. The FRS 3 loss per share (which is after taking account of goodwill amortisation and exceptional items) was (66.4p) (2003: earnings of 10.5p).

Cash flow and borrowings

Closing net borrowings for the Group amounted to £84.6m (2003: £89.3m) a reduction of £4.7m. Cash flow from operations amounted to £29.6m (2003: £25.0m) with debtors continuing to reduce in absolute terms with the fall in turnover.

Net capital expenditure was £2.6m (2003: £5.7m) and was largely to support IT systems developments, with no major capital projects undertaken in the year.

Financial and operational controls have continued to be strengthened across the Group. The procedures to monitor and manage key risks have been used throughout the year and enhanced further.

Financial Review continued

Capital expenditure is expected to remain below the level of depreciation for the foreseeable future.

Dividends, interest and corporation tax amounted to a net payment of £14.8m (2003: £17.8m).

Equity shareholders' funds

Equity shareholders' funds reduced from £89.0m reported in 2003 to £29.5m, due largely to the negative impact of the exceptional items totalling £62.0m.

Acquisitions

Five businesses were acquired during the year at a cost of £2.5m with a further £0.2m potentially payable, subject to performance. In addition, a further £2.1m was paid as deferred consideration in respect of acquisitions made in 2003. In January 2005, the Group completed the acquisition of eight social care branches from Community Careline Services Limited at a cost of £1.6m, with potential additional deferred consideration of £0.2m.

Pensions

In accordance with FRS17, Retirement Benefits, the Group is required to compare the market value of its two defined benefit pension funds' assets at the year-end with the actuarial liabilities of those funds. At 31st December 2004, the pension funds' assets amounted to a total of £23.5m (2003: £19.7m) compared with total liabilities of £38.7m (2003: £35.4m), a net aggregate deficit of £15.2m (2003: £15.7m) of which £4.2m (2003: £4.4m) relates to the formal valuation of the Healthcall Scheme at the date of acquisition and which was recognised as a liability and treated as a fair value adjustment. In accordance with the transitional arrangements of FRS17, the remaining deficit of £11.0m has not been recognised on the balance sheet. The £4.2m liability is being met by future annual payments of £500,000 until 2015, whilst the remaining deficit is being met by higher employer contributions in the case of the Nestor Scheme and possible future contributions to be determined at the next actuarial valuation of the Healthcall Scheme.

Treasury management and financial instruments

Financial instruments include all assets and liabilities of a financial nature such as cash, loans, finance leases, overdrafts and long term liabilities. All such instruments play an important part in the operations of the Group to enable it to operate smoothly and efficiently and to pay its obligations as they fall due. They also enable the Group to fulfil its investment strategy including making appropriate acquisitions. The Group's objective is to use financial instruments to minimise the cost of capital at an acceptably low financial risk and to maximise flexibility to take advantage of investment and acquisition opportunities as they arise.

The Group is primarily a UK Healthcare business and does not have significant exposure to foreign exchange risks. Nevertheless the Group's strategy is to hedge its foreign exchange exposure where it arises with foreign currency loans or forward exchange contracts as appropriate.

The main risks arising from the Group's financial instruments are interest rate and liquidity risks. The Board considers each of these risks on a regular basis and the Group's stance towards each of these risks has remained unchanged.

The Group currently has in place £100.0m of committed borrowing facilities at a margin of 0.75% above LIBOR and due for repayment during 2006. In addition, uncommitted overdraft facilities of £5.0m were renewed during the year. At the end of the year, the Group had borrowings less cash of £84.6m (2002: £89.3m) and undrawn committed borrowing facilities of £16.0m. It is, and has been throughout the year, the Group's policy that no trading in financial instruments will be undertaken.

The Group entered into a hedging arrangement in November 2002 which has the effect of fixing £35m of its borrowing within an acceptable range of interest rates for four years.

Controls

Financial and operational controls have continued to be strengthened across the Group. The procedures to monitor and manage key risks have been used throughout the year and enhanced further. The Group's internal audit function was brought in-house during the year having previously been provided by Deloitte & Touche.

International Financial Reporting Standards

In June 2002, the Council of the European Union adopted a Regulation requiring listed companies in its Member States to prepare their consolidated financial statements in accordance with International Accounting Standards from 2005. The first financial results announcement prepared in accordance with IFRS will be that for the first half of 2005. The first Annual Report prepared under IFRS will be that for the year ending 31st December 2005. The Group's project to convert its financial reporting from UK GAAP to IFRS is underway. Restated summary financial statements for the year ended 31st December 2004 (without comparatives for the year ended 31st December 2003) will be prepared ahead of the results announcement for the first half of 2005.

Martyn Ellis, Finance Director
7th March 2005

Clinical Governance

Clinical Governance
Despite the difficult trading conditions encountered, the Group continues to adopt a robust approach to the identification and management of clinical risk. This process is overseen by the Clinical Risk Management Group, an internal committee of senior staff. In addition we have the benefit of a Clinical Advisory Board, comprising eminent healthcare practitioners, who are independent of the Group.

Increasing health and social care regulation continues to impact upon the Group's services. We recognise government's desire to ensure the safety and accountability of clinical services, and seek to make our contribution by meeting externally accepted standards. The Group can report further progress.

Primary Care has undergone a fundamental change, with the transfer of contracted responsibility for out-of-hours care from GPs to Primary Care Trusts. Those contracts bring security, but also higher performance and reporting standards. There has been some public anxiety that this change has weakened relationships between doctor and patient, and some corresponding adverse press comment. Our performance against those targets has continued to improve, and measures of patient satisfaction are reassuring.

In Primecare Forensic (Police) and Primecare Primary Care, we have grown the traditional role of nurses, demonstrating their ability, with appropriate training and supervision, to undertake a proportion of the tasks currently undertaken by doctors, where the level of available resource continues to be a concern.

In domiciliary care, we continue to work hard to ensure that we meet fully the statutory and regulatory requirements to protect the elderly and vulnerable.

We believe our adverse incident reporting has been efficient, and our whistleblowing policy, though used only rarely, appears effective and valued. Both reflect well on the guidance provided by our Clinical Advisory Board, to the members of which we add our thanks. One year ago, we acknowledged that the time and resources for clinical governance require continued commitment from the Group. These tasks remain central to controlling clinical risk, and satisfying external scrutiny. We continue to believe that they add shareholder value by meeting those important objectives and contributing to the delivery of an advantage in the market place wholly consistent with high quality patient care.

We continue to believe that committing time and resources to clinical governance adds shareholder value and creates an advantage in the marketplace.

The Group is always looking for new ways in which to involve its employees in the communities in which they are based. A number of successful programmes were run throughout 2004.

Employee involvement
The Group believes that involving its employees in all aspects of its business, particularly the economic and financial factors affecting the Group's performance, is crucial to its future success. It is always seeking ways to improve communication across its businesses, both between its central and operational functions and between the various operations themselves.

Established consultative arrangements with elected representatives of employees have been used extensively throughout 2004, as a means of imparting knowledge and information to employees, particularly where there have been significant changes during the year.

It is the Group's policy to encourage employees to participate in its success, through a variety of performance-related incentive arrangements, including the provision of savings-related share option schemes.

Internal newsletters are issued regularly, increasingly through the use of new media to reach all staff faster and more efficiently. In 2004, the Group further improved its IT infrastructure, in order to ensure that timely and comprehensive information reaches its employees on a regular basis. Its key policies and procedures are published on a Group-wide intranet, which is available to all staff, and the intranet homepage contains relevant and up-to date information of interest on a real-time basis.

Diversity and training
The Group recognises its responsibilities in this key area of working life and is continually taking steps to balance society and employee needs with its business requirements. It has a wide and varied employee base with significant numbers of female employees, many at senior management level, as well as a significant employee base of individuals who come from ethnic minority groupings.

The programme to actively recruit employees with disabilities, particularly in the Birmingham Clinical Response Centre, commenced in 2003 and was continued in 2004, although inevitably impacted by the number of redundancies necessitated by the decision of many PCTs to use alternative solutions for their out-of-hours primary care needs. The Group also implemented a number of changes to its operational working practices and policies in order to ensure compliance with the Disability Discrimination Act 1995, which came into force in October.

The Group continues to refine its systems to capture the diversity of the Group and seeks innovative methods of attracting scarce clinical and carer resource, including the provision of proven computer diagnostic software enabling clinicians to provide clinical advice from their own homes and operational processes to facilitate part-time working.

In the Group's staffing businesses, the requirements of legislation, particularly the Care Standards Act 2000, and of its key customers have led to the development of comprehensive training development programmes for both employees and the health and care professionals who help to provide the Group's services. These programmes are delivered by a combination of in-house and externally-based training organisations and support the high levels of service offered by the Group.

Health and Safety
The Board is aware of its responsibilities towards its employees and all users of the Group's services in health and safety matters. It recognises its ultimate responsibility for the setting and monitoring of appropriate policies, guidelines and practices in the formal Schedule of Matters Reserved for the Board's consideration.

The Group's Director of Human Resources is directly accountable to the Chief Executive for overseeing safety matters and in 2004 has worked closely with the Group's business units to roll out revised policies and reporting arrangements.

An ongoing training programme supports the effective implementation of this process which is based on a comprehensive series of risk assessments and reporting arrangements under the day-to-day direction of a dedicated health and safety manager.

In 2005, the Group plans to integrate all health and safety matters into the Nestor Quality Management System, which is currently undergoing trial.

Charity of the Year
As part of its commitment to UK health and social care, the Group asks many of its branches every year to vote for the organisation or charity they would like to support as Charity of the Year.

Throughout 2004, the Group supported fundraising activities on behalf of the Christian Lewis Trust. This is a UK charity supporting children with cancer and their families.

The Group is always looking for new ways in which to involve its employees in the

communities in which they are based. A number of successful programmes were run throughout 2004. It also initiated a number of projects intended to benefit the environment as well as raise funds for charitable causes, such as recycling used toner cartridges. Throughout the UK, the Group's branches regularly support charities pertinent to their own locality or business sector, as well as the Charity of the Year.

Environmental policy

As a service-based organisation, with no manufacturing, limited transportation facilities and no freehold properties, the Group's exposure to environmental risk is limited, as is its ability to control the environmental impact of its activities.

However, the Group and its businesses are committed to following the best environmental practices in the day-to-day conduct of their business and the management of their resources and facilities. During the year, the Group continued to refine the formal environmental policy adopted by the Board in 2000, with a particular focus on newly acquired businesses and on matters relating to the clinical services provided by the Group. The policy document, which is directed at minimising the potential impact of the Group's operations on the environment, provides that the Group's Board retains ultimate responsibility for setting and monitoring its policy on environmental matters.

The policy provides for the promotion of an understanding of environmental consideration across the Group and all managers are directed to encourage staff to follow the good practice outlined in the policy at all times.

The aims of the Group's environmental policy are:

- to take all practical steps to ensure the Group's business activities have the minimum negative impact on the environment
- to achieve the most economic and careful use of sources of fuel and energy
- to minimise the production of waste and to manage the disposal of clinical waste in a safe manner
- to make the maximum practical use of recycling.

Responsibility for the co-ordination of the policy throughout the Group rests with the Board, with the Chief Executive having specific responsibility. The policy is administered by the Group's Director of Human Resources, who coordinates the activities of various relevant Group functions.

Specialist advisors are appointed by the Director of Human Resources as required to ensure that best practice is followed, that the Group is aware of potential opportunities to improve performance and that all legislative and statutory requirements are met.

The directors of the Group's operating companies are responsible for ensuring compliance with the policy. Where appropriate, departmental representatives or co-ordinators have been appointed to act as a focal point for the dissemination of information and the promotion of initiatives to improve the immediate environment, reducing waste and ensuring that the objectives of the policy are met. Where practicable, paper and other consumables are recycled and all employees are encouraged to operate the business in as environmentally-friendly a manner as possible.

Ethical matters

The Board has adopted a formal Code of Business Conduct, covering all the businesses in the Group, which has consolidated all of the various codes previously applicable to them. The Code provides comprehensive guidelines to all employees and "members" as to the standard of business ethics expected from them as representatives of the Group. It also recognises the importance to the Group of operating to the highest possible ethical standards, bearing in mind the nature of the services offered by Group companies and the needs of their clients.

The Group operates two comprehensive whistleblowing policies, in respect of clinical issues and general operational and financial matters.

At the Group's Business Resource Centre in Hatfield, most gifts received by members of staff from suppliers and potential suppliers are auctioned amongst all staff (where practicable) and the proceeds of such auctions are donated to the Group's Charity of the Year.

All senior managers are required to declare, on an annual basis, any hospitality received during the year in their capacity as employees of the Group and to disclose any interests they may have in connected or competing organisations. These declarations are monitored by the Group Company Secretary and reported to the Board at the end of each year.

All Board members are required, once a year, to submit their annual expense claims to the scrutiny of the entire Board.

Emma Thomas,
Group Company Secretary

Board of Directors

1 John Rennocks
Chairman

(59), joined the Group and was appointed to the Board as Chairman in October 2003. A chartered accountant, he is also non-executive chairman of Diploma plc and holds a number of non-executive appointments in a broad range of companies including Foreign & Colonial Investment Trust plc, Babcock International Group plc and Wagon plc.

Previously, he was Executive Director, Finance of Corus Group plc (formerly British Steel plc) between 1996 and 2001. From 1989 to 1996 he was Finance Director of Powergen plc and prior to that Finance Director and Company Secretary of Smith & Nephew plc.

He is Chairman of the Board's Nomination Committee and a member of its Audit and Remuneration Committees.

2 Stephen Booty
Chief Executive

(50), was appointed to the Board as an Executive Director in June 2002, having joined the Group in January 2002, as Managing Director, Healthcare Personnel Division. He was appointed Acting Chief Executive in May 2004 and Chief Executive in December 2004.

He has over twenty years experience in the fast moving consumer goods sector, working for blue chip organisations, marketing branded goods and driving efficiencies through innovative business processes. His previous roles include Chief Operating Officer, Europe at Chep International and senior sales, management and operational roles at Kimberly-Clark and Scott Paper.

3 Martyn Ellis
Finance Director

(48), joined the Group and was appointed to the Board in May 2003. A cost and management accountant, he previously held positions as Finance Director of TeleCity plc, Whitecroft plc, Mann Egerton and Campbell Foods (UK).

4 Roger Dye
Non-Executive Director

(53), was appointed to the Board as a non-executive director in January 2004. A chartered accountant, he has been Finance Director of the Davis Service Group since August 2000 and will become its Chief Executive from May 2005. Previously, he was Group Finance Director of Transport Development Group plc, Cray Electronics plc and Domino Printing Sciences plc.

He is Chairman of the Board's Audit Committee and serves on its Nomination and Remuneration Committees.

5 Dr William Holmes
Executive Director

(50), was appointed to the Board as a non-executive director in January 2000 and as the Group's executive Medical Director in October 2001. His executive responsibilities include the developing and monitoring of clinical standards and leading a team to provide clinical governance across the Group. He is a Fellow of the Royal College of Physicians of London and a Fellow of the Royal College of General Practitioners. In addition to his corporate responsibilities, he continues to undertake regular clinical sessions in occupational medicine.

6 Sir Andrew Foster
Non-Executive Director

(60), was appointed to the Board in January 2004. He has had a long and distinguished career in public service, having served as Chief Executive of the Audit Commission for England & Wales between 1992 and 2003. Other previous appointments include Deputy Chief Executive of the NHS and Director of Social Services for North Yorkshire County Council. He is now Deputy Chairman of the Royal Bank of Canada Europe Ltd., a non-executive director of the Sports' Council and has a range of positions in the public and private sectors.

He is the senior non-executive director and Chairman of the Board's Remuneration Committee. He is also a member of its Nomination and Audit Committees.

7 Ingrid Alexander, CBE
Non-Executive Director

(53), was appointed to the Board in August 2001. An independent management consultant, she was the final Chairperson of the Central Council for Education and Training in Social Work and a member of the Kings Fund Grants Committee. She is a former member of the General Social Care Council Advisory Group and the Strategy Group for the NHS Chief Executive's leadership programme and has worked widely with a number of other organisations in the health and social care field. Previously, she was Assistant Director for Resources at Birmingham City Council.

She is a member of the Board's Nomination, Audit and Remuneration Committees.

Directors' Report

The directors are pleased to present their report and the audited financial statements for the year ended 31st December 2004.

Principal activities, results and future developments
Nestor Healthcare Group plc is the holding company of a group of companies in the healthcare sector. Its principal activities are organised into three business units. These comprise:

- Healthcare Staffing – the provision of nurses and carers, locum doctors and other medical personnel;
- Social Care – the provision of home and social care personnel and services through a network of company owned and franchise branches across the UK; and
- Primary Care – the provision of GP and other out-of-hours services to the NHS, the provision of medical staff to the Benefits Agency Medical Services and the provision of healthcare and related services to Police Authorities and secure institutions.

The Chairman's Statement, Chief Executive's Review and Financial Review on pages 1 to 8 provide a report on the Group's activities, trading results and future developments.

Results and dividends
The loss attributable to shareholders was £58,190,000 (2003: profit of £9,202,000). No interim dividend was paid during the year but the directors now recommend a final dividend of 1.50 pence per ordinary share, to be paid to shareholders on 3rd June 2005. Following payment of all dividends for the year, totalling 1.50 pence, the loss of £59,504,000 will be transferred from the Group's reserves.

Directors
The directors who served during the year were Ingrid Alexander, Stephen Booty, Roger Dye, Martyn Ellis, Sir Andrew Foster, William Holmes, John Rennocks, Justin Jewitt, Robert Nicholls and Stephen Page.

Robert Nicholls retired from the Board on 19th January 2004; Roger Dye and Sir Andrew Foster were appointed as independent non-executive directors on the same date. Justin Jewitt resigned as a director on 27th May 2004 and Stephen Page resigned as a director on 3rd August 2004.

In accordance with the Articles of Association, Stephen Booty, Martyn Ellis and William Holmes will retire by rotation at the Annual General Meeting and, being eligible, will offer themselves for re-election.

Stephen Booty, Martyn Ellis and William Holmes each has a service agreement with the Company, further details of which are provided at page 20 in the Remuneration Report.

Directors' interests
All directors' interests, including details of shareholdings, are set out in the Remuneration Report of the Board on pages 17 to 23.

Substantial shareholdings
At the date of this report the Company has been notified of the following material interests of 3% or more and non-material interests of 10% or more in its ordinary share capital:

Shareholder	Number of shares	Percentage of issued share capital
Schroder Investment Management Limited	22,784,770	26.00%
Aberforth Smaller Companies Trust plc	3,040,800	3.47%
AVIVA plc	2,772,391	3.16%
The Capital Group Companies, Inc.	2,679,009	3.06%

Details of the authorised and issued share capital of the Company during the year ended 31st December 2004 are given in note 23 to the financial statements.

Annual General Meeting – special business

The Annual General Meeting of the Company will take place at UBS Investment Bank, 1 Finsbury Avenue, London EC2M 2PP on Thursday, 28th April 2005 at 12.00 noon. The notice of the Annual General Meeting may be found in the Notice of Meeting accompanying this Report. In addition to the routine business of the meeting, the following special business will be transacted:

- Directors' authority to issue shares (Resolution 8)

  The Companies Act 1985 ("the Act") prevents directors from allotting unissued securities without the authority of shareholders. In certain circumstances this could be unduly restrictive. The proposed resolution will give the directors a general authority to issue shares of the Company for cash, within certain constraints, without complying with the statutory pre-emption procedures. The total number of relevant shares that the directors will have the authority to allot will be 8,300,000 ordinary shares of 10p each (representing 9.5% of the share capital currently in issue). The directors have no present intention to exercise this authority (except in relation to the allotment of shares under the Group's share option schemes). The authority in Resolution 8 will expire at the conclusion of the next Annual General Meeting or on 28th July 2006, whichever is the earlier.

- Restricted disapplication of pre-emption rights (Resolution 9)

  The proposed special resolution will give the directors a limited authority to issue equity shares for cash other than to existing shareholders in proportion to their existing shareholdings notwithstanding the pre-emption provisions of Section 89 of the Act. This limited authority would allow the directors to make such issues provided they do not exceed in aggregate an amount equal to 5% of the issued share capital of the Company. The resolution also contains provisions enabling the directors to take action to overcome certain practical difficulties that could arise in the case of a rights issue. The authority in Resolution 9 will expire on the conclusion of the next Annual General Meeting or on 28th July 2006, whichever is the earlier.

- Purchase by the Company of its own shares (Resolution 10)

  The directors consider that it would be advantageous for the Company to renew for a further year the existing authority granted at last year's Annual General Meeting, to allow the use of the Company's available cash resources to acquire its own shares in the market for cancellation. This authority is granted pursuant to Section 162 of the Act.

  Accordingly, a special resolution is proposed to authorise the purchase in the market of up to 10% of the issued ordinary shares of the Company at a price of not more than 105% of the average of the middle market quotations for the ordinary shares of the Company (as derived from the London Stock Exchange Daily Official List) for the ten business days prior to the date of purchase.

  The directors do not intend to exercise the Company's power to purchase its own shares other than in circumstances where they consider this to be in the shareholders' interests and where this would result in an increase in earnings per share. They have no present intention to exercise this authority.

Charitable and political donations

No political donations were made during the year (2003: £nil). Charitable donations of £3,600 were made to various charities in 2004 (2003: £100).

Taxation status

The Company is not a close company within the meaning of the Income and Corporation Taxes Act 1988.

Disabled employees

It is the Group's policy that disabled persons should be considered for employment, training, career development and promotion on the basis of their abilities and aptitudes in common with all employees.

The Group applies employment policies that are fair and equitable for all employees and which ensure that entry into and progression within the Group are determined solely by application of job criteria and personal ability and competency.

Full and fair consideration (having regard to the person's particular aptitudes and abilities) is given to applications for employment and the career development of disabled persons. The Group's training and development policies make it clear that the Group will take all steps practicable to ensure that employees who become disabled during the time they are employed by the Group are able to continue to perform their duties.

Employee involvement

The Group attaches considerable importance to ensuring that all its employees are provided with information concerning them as employees, particularly the economic and financial factors affecting the Group's performance and the market in which the Group operates. Involvement of employees in the Group's performance is also encouraged by the availability of performance-related bonuses as well as share option schemes, which are described in more detail elsewhere in this report.

Directors' Report continued

Employee involvement continued
Internal circulars and newsletters are issued on a monthly basis and consultation between management and staff is an ongoing process. Employees are consulted on issues directly affecting them wherever practicable. Further details of the Group's policies and practices relating to employee involvement may be found on page 10 to this report.

Creditor payment policy
It is the Group's policy to have appropriate terms and conditions for transactions with suppliers, ranging from standard terms and conditions to those which have been specifically negotiated, and that in the absence of dispute, payment will be made in accordance with those terms and conditions and conforming to the CBI Code of Best Practice; copies are available from the CBI at Centrepoint, 103 New Oxford Street, London. At 31st December 2004 trade creditors represented eleven days' purchases (2003: nine days).

The directors' reports of the Group's United Kingdom operating companies give information about their creditor payment policies as required by the Companies Act. The Company, as a holding company, does not itself make any relevant payments in this respect.

Auditors
A resolution proposing the reappointment of PricewaterhouseCoopers LLP, Chartered Accountants, as auditors to the Company and authorising the Audit Committee of the Board to determine their remuneration will be put to the Annual General Meeting.

Approved by the Board on 7th March 2005 and signed on its behalf by:

Emma Thomas
Group Company Secretary

Nestor Healthcare Group plc
Registered number 1992981

Directors' Responsibilities

In respect of the preparation of financial statements:
The directors are required by company law to prepare financial statements which give a true and fair view of the state of affairs of the Company and the Group at the end of the financial year and of the profit and cash flows of the Group for the period to that date.

The financial statements must be prepared in compliance with the required formats and disclosures of the Companies Act 1985 and in accordance with applicable accounting standards. In addition, the directors are required:

- to adopt suitable accounting policies and apply them consistently;
- to make judgements and estimates that are reasonable and prudent;
- to take account of expenses and income relating to the period being reported on, whether or not they have been paid or received in that period; and
- to prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors confirm that the financial statements comply with the above requirements.

The directors are also responsible for the maintenance and integrity of the Nestor Healthcare Group plc web sites on which the financial statements are published. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The directors are also responsible for maintaining adequate accounting records so as to ensure that the financial statements comply with the requirements of the Companies Act, for safeguarding the assets of the Group, and for preventing and detecting fraud and other irregularities.

Remuneration Report

The Board is pleased to present its remuneration report for the year ended 31st December 2004.

Remuneration Committee (non-audited)
During the year, the Board delegated its powers to determine the Company's remuneration policy for senior executives, including executive directors, to the Remuneration Committee ("the Committee"), the members of which during the year were Sir Andrew Foster (Chairman from 19th January 2004), Ingrid Alexander, Roger Dye, all of whom are regarded by the Board as independent non-executive directors and John Rennocks (who was regarded by the Board as being independent within the meaning of the Code, on the date of his appointment). The Board has retained responsibility for setting the remuneration of the Company's Chairman since he currently serves as a member of the Committee. Robert Nicholls acted as Chairman of the Committee until his retirement from the Board on 19th January 2004.

The terms of reference of the Committee may be found on the Company's website. Further details relating to the Committee may be found on page 26 of this report.

In determining its policy, the Committee has paid regard to the principles and provisions of good governance contained in the Code on Corporate Governance published in July 2003 ("the Code") and to the Directors' Remuneration Regulations 2002. It has also received advice on executive remuneration from New Bridge Street Consultants LLP ("NBSC"), which during the year was retained by the Committee as its regular advisor. A copy of a statement relating to the terms on which NBSC is engaged by the Committee is available on the Company's website. The Committee has also received assistance from Stephen Booty, the Group's Chief Executive, James Buchanan, the Group's Director of Human Resources and Emma Thomas, the Group Company Secretary, all of whom attend meetings of the Committee as required but not in respect of matters relating directly to their own remuneration. Prior to his resignation on 27th May 2004, Justin Jewitt, the Company's previous Chief Executive also provided assistance to the Committee.

The Company has also instructed NBSC to advise it on certain ad hoc matters during the year, for example in relation to certain pension matters and the administration of the Company's share schemes.

Remuneration Policy (non-audited)
The Committee's overall aim is to provide a package of remuneration which:

- is sufficient but no more than is necessary to attract, retain and motivate all of the Company's most senior management, including executive directors;
- rewards good performance with remuneration that is in line with that payable in broadly comparable businesses; and
- rewards exceptional performance in such a way as to align the executives' interests with those of the Group's shareholders.

To that end, the Committee structures executive remuneration in two distinct parts: fixed remuneration of basic salary and benefits and variable performance-related remuneration, in the form of a cash bonus and long-term incentives. Remuneration is structured so that the variable pay element forms a significant portion of each director's package.

Basic salary and benefits
Basic salary is determined by reference to the responsibilities and performance of the individual directors during the year, taking into account experience and the rates of basic pay for similar roles in comparable companies. The Committee's overall aim is to ensure that the basic salary paid to the Group's senior executives is broadly in line with the median of that paid by comparable businesses, having particular regard to their size and complexity. Salaries are reviewed annually, normally in November or December of each year and any adjustments usually take effect from 1st January in the following year. It is the Committee's practice to undertake formal market benchmarking of directors' and senior executives' salaries, with the assistance of NBSC, every two years. With effect from 1st January 2005, executive directors' basic salaries will range from £160,000 to £300,000. The Company additionally provides a range of benefits to executive directors, the most significant of which are a fully expensed car or cash alternative and pension benefits (full details of which are set out below).

Cash bonus
Each year, the Committee sets stretching bonus targets for each executive, aiming to achieve a balance between short and medium-term objectives. In 2005, targets comprise overall Company performance criteria relating to profit before tax. In the scheme in operation during 2004, the bonuses for executive directors were based on a combination of the achievement of specific profit targets (earnings for the Group as a whole and profits of each business unit where appropriate) and the achievement of personal targets aligned to those areas for which they were specifically responsible. Up to 80% of the total maximum bonus was payable in respect of financial targets and up to 20% of the total maximum bonus was payable if the executive met all of his personal objectives in full. No bonus was payable if the relevant financial targets were not met, even if the executive director had met his personal objectives in full.

The maximum such annual bonus payable to executive directors is 80% of salary, except that payable to William Holmes, which is 50% of salary. Directors who are eligible to receive a maximum annual bonus of 80% are required to invest one half of their post-tax receipt into the Company's Long Term Incentive Plan ("LTIP"). Details of the LTIP are provided later in this report. Bonuses are not pensionable.

Remuneration Report continued

Long-Term Incentives

The Company currently operates two long-term incentive schemes, the Nestor Healthcare Group Share Option Plan 2002 ("the 2002 Plan") and the LTIP, both of which were adopted following approval by shareholders in 2002. In proposing the schemes, the Committee took extensive advice from NBSC, sought and obtained the prior approval of a number of the Company's largest shareholders and complied with prevailing best practice relating to such arrangements.

i. The 2002 Plan

The Committee believes that share ownership by senior executives is an effective means of rewarding superior performance, since the interests of management and shareholders are thereby aligned. The Committee further believes that the provision of share schemes to the Group's managers should be structured in such a way as to encourage them to achieve the Group's long-term aims and that the Group's most senior managers, including executive directors, should be rewarded for exceptional performance with potentially significant rewards.

It is generally the Company's policy, therefore, to grant share options regularly, on a tiered basis, to a broad range of middle and senior management, including executive directors. In previous years, options have been granted annually to executive directors, to a value equivalent to one times salary, although in exceptional cases, where a key executive joins the Group, a higher limit has sometimes been applied. In other years, a lower limit has also been applied and in 2004 no share options were granted under the 2002 Plan.

"Normal" options

For "normal" options granted to the Group's most senior executives, including all executive directors, a range of normalised earnings per share ("EPS") performance targets will apply to grants as shown below:

	Average growth required in EPS
1st third of an option	RPI + 5% pa
2nd third of an option	RPI + 6% pa
Final third of an option	RPI + 10% pa

In all cases, performance is tested over a three-year period. Since January 2004, the Committee has resolved that there will be no opportunities to re-test performance for grants made after that date.

EPS was chosen as the relevant benchmark for the measurement of the Company's performance since the target requires substantial improvement in underlying financial performance before options may be exercised. This complements the requirement inherent in an option, which is to grow the share price. The range of EPS targets are considered to be appropriately stretching, generating higher potential reward levels for higher levels of financial performance. This benchmark will continue to be kept under review.

No options were granted during the year under this scheme.

"Super" options

In addition to "normal" options, the 2002 Plan also provides for the grant of "super" options to certain of the Group's most senior managers, including executive directors. The Committee does not intend to grant these "super" options to those executive directors who are eligible to receive LTIP awards but may grant such options to William Holmes, who is not. These options may be granted over shares worth up to one and a half times the individual's salary and the exercise of these options is subject to the achievement of more stretching targets than those prescribed by the Committee in relation to "normal" options.

Performance targets relating to "super" options involve a comparison of the Company's total shareholder return ("TSR") with companies in the FTSE Mid 250 index (excluding investment trusts) as at the date of grant, measured over a single three year period from grant. Options are exercisable as set out below:

Nestor's TSR ranking in group	% of "super" options exercisable
Below 45th percentile	0%
45th percentile	40%
45th percentile to 25th percentile	Sliding scale from 40% to 100%
25th percentile and above	100%

In addition to the TSR condition above, no element of the option is exercisable unless the Company's EPS growth over the three-year period exceeds 5% per annum over RPI. There is no opportunity to re-test performance.

No options were granted during the year under this scheme.

ii. LTIP

Under the LTIP, the executive directors who are eligible to participate (namely Stephen Booty and Martyn Ellis) are required to invest one half of their post-tax cash bonus in buying shares in the Company. The investment will be matched by the grant of matching awards.

Matching awards will normally only vest on the third anniversary of their grant if the participant is still in the Company's employment, has retained the shares purchased with the bonus and if specified performance targets are met. The current performance target involves a comparison of the Company's TSR with companies in the FTSE Mid 250 index (excluding investment trusts) as at the date of grant, measured over a single three year period from grant. Matching awards vest as set out below:

	Matching Ratio	
Nestor's TSR ranking in group	Chief Executive	Other Eligible Executive Directors
Below 45th percentile	0	0
45th percentile	0.5:1	0.3:1
45th percentile to 10th percentile	Sliding scale from 0.5:1 to 4:1	Sliding scale from 0.3:1 to 2.5:1
10th percentile and above	4:1	2.5:1

In addition to the TSR condition above, none of the award will vest if the Company's EPS growth does not exceed the growth in RPI by an average of at least 5% per annum over the three year period. There is no opportunity to re-test performance.

The Committee considers TSR to be a suitable performance measure for both the "super" options and the LTIP as it clearly aligns interests of shareholders and executives. It also considers that the FTSE Mid 250 Index is an appropriate benchmark as there are no other companies with a similar business profile to the Company listed on the UK Stock Exchange. TSR performance will be independently calculated for the Committee. A chart showing the Company's TSR compared to the FTSE Mid 250 Index over the last five financial years is shown below.

Participation in the matching awards to date has been as follows:

	Number of shares notionally held at 01.01.04	Notionally awarded in the year	Vested in the year	Lapsed in the year	Potential interest in shares at 31.12.04	Share price at date of notional award (p)	Amount charged against profit in the year £000	Earliest vesting date
Stephen Booty	–	33,108	–	–	33,108	185.0	–	07.04.07
Martyn Ellis	–	22,297	–	–	22,297	185.0	–	07.04.07
Justin Jewitt	–	54,054	–	54,054	–	185.0	–	
Stephen Page	–	15,589	–	15,589	–	185.0	–	
Total directors	–	125,048	–	69,643	55,405		–	

iii. SAYE Scheme

The Company also operates a savings related share option scheme, which provides a long-term savings opportunity for all of the Group's employees, as well as encouraging them to participate in the success of the Company. Participation is open to all permanent employees who are able to make regular monthly savings and are exercisable in normal circumstances after three or five years at a price which is fixed at a discount of 20% from the average of the mid-market prices for the five business days immediately preceding the date on which invitations are made by the Committee.

iv Share Price Linked Scheme

In December 2004, the Company established a phantom long-term incentive arrangement for the benefit of the Chief Executive, designed further to align his interests with those of the company in the light of the significant challenges presented by the changes in the market in which the Company now operates. The scheme provides for the grant of 477,137 notional "phantom" options over the Company's shares, which are exercisable in up to two equal tranches, provided the Company achieves challenging profit before tax targets in 2005 and 2006 respectively, at any time after the performance conditions have been met before 14th December 2007. The maximum amount payable under this scheme to the Chief Executive is £500,000 and the value of the award is entirely dependent upon an increase in the Company's share price from the exercise price, the prevailing mid-market price at the date of grant being 125.75 pence.

Company policy on the pensions of executive directors (non-audited)

Until it was closed to new entrants in April 2003, executive directors were able to join the Nestor Healthcare Group Retirement Benefits Scheme ("the Scheme"), a funded, Inland Revenue approved, final salary occupational pension scheme. Pensions in the Scheme are based on final salary (excluding bonuses) and length of pensionable service. In respect of those directors who are members of the Scheme, the Company has agreed to provide benefits based on their actual basic salary, even where this exceeds the Inland Revenue Earnings "cap", subject to their making members' contributions to the Scheme on the same basis. The Company has also established an unapproved scheme to provide additional death-in-service benefits to these directors in line with their actual basic salaries.

Under the Scheme, the normal retirement age of executive directors is 60 and the basic rate of accrual is 1/50th.

Stephen Booty also receives a cash sum to enhance these benefits to an accrual rate of 1/30th.

Since the Scheme was closed to new entrants in April 2003, newly appointed employees, including executive directors, are eligible to join the Nestor Healthcare Group Personal Pension Plan ("GPP"), which is a defined contribution arrangement. In respect of executive directors, the Company makes contributions to the GPP at a rate (subject to Inland Revenue capped limits) up to a maximum of 20% of the director's basic salary. If a director is eligible to have contributions at a rate of 20% of his basic salary paid by the Company, but such payment would be in excess of the Inland Revenue capped limits, then any shortfall is instead paid to the director in cash (taxed in the normal way) as compensation in lieu of pension contributions.

Executive directors' contracts of service (non-audited)

Policy

It is the Committee's policy only to offer contracts terminable on no more than 12 months' notice to executive directors. All currently serving executive directors have contracts of employment terminable in all circumstances on a maximum of 12 months' notice. When offering contracts of employment to newly appointed executive directors, the Committee has regard to the broad principles outlined in the ABI and NAPF's joint statement on Best Practice on Executive Contracts and Severance, including the director's duty to mitigate his losses in the event of early termination of his contract.

Specific Contractual Details

Current executive directors

			Termination provisions		
	Date of contract	Notice period	"Pay in lieu of notice" clause	Share Options	Annual Bonus
Stephen Booty	1st February 2003	12 months' notice from Company	Note 1	Note 2	Note 3
Martyn Ellis	23rd May 2003	12 months' notice from Company	Note 1	Note 2	Note 3
William Holmes	1st October 2001	12 months' notice from Company	Note 1	Note 2	Note 3
Former executive directors					
Justin Jewitt	20th March 1997	12 months' notice from Company	Note 1	Note 2	Note 3
Stephen Page	18th July 2001	12 months' notice from Company	Note 1	Note 2	Note 3

Notes

1 The Company may terminate the director's employment without notice, provided it pays to him an amount equating to his salary, benefits and employer's pension contributions or credits him with an additional period of pensionable service (as applicable) for the unexpired period of notice due under the contract. Martyn Ellis's contract permits the Company to pay any monies due on a monthly basis and, at its discretion, to cease or reduce payments if he accepts suitable alternative employment.

2 At the Board's discretion, the director may be entitled to retain any vested share options held under the Group's Share Option Schemes for a period of up to 12 months from termination. He may also be entitled to exercise unvested share options early in certain specified circumstances subject to the Committee taking account of the performance of the Company and the length of time elapsed since the grant date.

3 Depending on the time of year at which his employment is terminated, the director may be entitled to any bonus earned by him (but not yet paid) under the Group's bonus scheme.

Chairman and non-executive directors (non-audited)

The Board sets the fee levels for the Chairman and non-executive directors. Non-executive directors do not hold contracts of employment but are offered letters of appointment for a fixed period of three years, renewable annually thereafter by agreement. Non-executive directors do not participate in any of the Group's annual or long-term incentive arrangements, nor is their remuneration pensionable.

Current non-executive directors

	Date of letter of appointment	Appointment term	Compensation in the event of early termination of office
John Rennocks	1st October 2003	3 years from 1st October 2003	3 months' fees
Ingrid Alexander	25th July 2001	3 years from 13th August 2001 (extendable by up to 3 further periods of 12 months each)	None
Roger Dye	9th January 2004	3 years from 1st January 2004	None
Sir Andrew Foster	16th January 2004	3 years from 1st January 2004	None

Former non-executive directors

	Date of letter of appointment	Date of leaving Board	Compensation in the event of early termination of office
Robert Nicholls	14th May 1997	19th January 2004	None

Directors' emoluments (audited)

	Basic salary and fees 2004 £000	Performance related bonuses 2004 £000	Taxable benefits 2004 £000	Compensation for loss of office (including pensions) 2004 £000	Total emoluments 2004 £000	Total emoluments 2003 £000
Ingrid Alexander	29	–	–	–	29	29
Stephen Booty	232	173	95	–	500	282
Roger Dye	33	–	–	–	33	-
Martyn Ellis	190	61	30	–	281	170
Sir Andrew Foster	33	–	–	–	33	-
William Holmes	160	32	18	–	210	174
John Rennocks	106	–	–	–	106	29
Justin Jewitt	129	–	18	370	517	322
Robert Nicholls	–	–	–	–	–	37
Stephen Page	115	–	19	204	338	205
Antony Beevor	–	–	–	–	–	80
Timothy Harris	–	–	–	–	–	26
David Howell	–	–	–	–	–	33
David Lyon	–	–	–	–	–	255
Total 2004	1,027	266	180	574	2,047	–
Total 2003	1,090	178	157	217	–	1,642

Benefits receivable consist primarily of company car provision or car allowance, car fuel and healthcare insurance.

50% of that element of the net (after tax) performance related bonuses that are applicable to the LTIP payable to Stephen Booty and Martyn Ellis are to be invested in the Group's shares in the LTIP, amounting to £24,000 and £18,000 for Stephen Booty and Martyn Ellis respectively.

Stephen Booty earned an additional bonus, separate from the annual bonus, which was paid on the achievement of specific targets set at the time of his appointment as Acting Chief Executive in May 2004. This additional bonus was not subject to the requirement to invest in the LTIP.

Included in compensation for loss of office for Justin Jewitt is an amount of £106,000 that has yet to be paid. It is expected that payment of this amount will be made during 2005.

Included in compensation for loss of office for Justin Jewitt is a payment of £75,000 representing additional pension contributions as provided for in his service agreement. Included in the compensation for loss of office for Stephen Page is a payment of £46,710 representing additional pension contributions as provided for in his service agreement.

Directors' emoluments (audited) continued

Included in taxable benefits relating to Stephen Booty is a payment of £79,347 representing compensation in lieu of pension contribution. Included in taxable benefits relating to Martyn Ellis is a payment of £17,533 representing compensation in lieu of pension contribution.

Martyn Ellis was appointed as a director on 1st May 2003. John Rennocks was appointed as a director on 1st October 2003. Roger Dye and Sir Andrew Foster were appointed as directors on 19th January 2004.

David Lyon resigned as a director on 1st May 2003. Antony Beevor resigned as a director on 1st October 2003; David Howell and Timothy Harris resigned as directors on 28th October 2003 and 3rd November 2003 respectively. Robert Nicholls resigned as a director on 19th January 2004. Justin Jewitt resigned as a director on 27th May 2004 and Stephen Page resigned as a director on 3rd August 2004.

The figures above represent emoluments earned as directors during the relevant financial year. All are paid in the year that they are earned, with the exception of bonuses, which are paid in the year following that in which they were earned.

Directors' pensions (audited)

Defined benefit scheme

	Accrued pension per annum at 31st December 2004 £000	Increase in accrued pension during 2004 £000	Increase in accrued pension per annum during 2004 excluding price inflation £000	Transfer value of accrued pension at 31st December 2004 £000	Transfer value of accrued pension at 31st December 2003 £000	Transfer value of the increase excluding price inflation less director's contributions £000	Increase in transfer value during 2004 less director's contributions £000
Stephen Booty	10	4	4	115	50	29	53
William Holmes	10	4	4	117	47	40	62
Stephen Page (resigned 3rd August 2004)	13	3	3	104	54	16	43

The transfer values have been calculated on the basis of actuarial advice in accordance with the Actuarial Guidance Note GN11. The above figures exclude any benefits derived from directors' additional voluntary contributions.

Defined contribution schemes

Employer contributions of £31,500 (2003: £66,296) were paid during the year to a personal pension plan for Justin Jewitt excluding additional contributions disclosed in the compensation for loss of office.
Employer contributions of £20,400 (2003: £13,200) were paid during the year to the GPP in respect of Martyn Ellis.

Directors' interests (audited)

The beneficial and family interests of directors in post at the year-end in the share capital of the Company according to the register of directors' interests maintained by the Company under Section 325 of the Companies Act 1985 were:

	Ordinary Shares (non-audited)		Share Options (audited)							
			Company Plan 1996		Employee Scheme 1996		Share Option Plan 2002		SAYE Schemes	
	31.12.04	31.12.03	31.12.04	31.12.03	31.12.04	31.12.03	31.12.04	31.12.03	31.12.04	31.12.03
Ingrid Alexander	–	–	–	–	–	–	–	–	–	–
Stephen Booty	57,814[3]	–	5,514	5,514	23,897	23,897	124,941[6]	124,941[6]	6,014	6,014
Roger Dye	–	–[5]	–	–[5]	–	–[5]		–[5]	–	[5]
Martyn Ellis	5,262[4]	–	–	–	–	–	64,716	64,716	–	–
Sir Andrew Foster	–	–[5]	–	–[5]	–	–[5]		–[5]	–	[5]
William Holmes	4,000	4,000	5,882	5,882	43,137	43,137	70,823	70,823	10,453	10,453
John Rennocks	4,896	4,896	–	–	–	–	–	–	–	–

Notes:

1 None of the directors has any non-beneficial interest in the Company's share capital.

2 No director was materially interested in any contract of significance (apart from contracts of service or for services) with any Group company during or at the end of the financial year.

3 Included in Stephen Booty's ordinary share holding is a total of 7,814 shares held under the LTIP.

4 All of Martyn Ellis's shares are held under the LTIP.

5 At date of appointment.

6 112,941 options granted to Stephen Booty under the 2002 Plan in 2002 are "Super Options".

7 On 7th January 2005, Stephen Booty, Martyn Ellis and William Holmes were granted 196,399 options, 128,314 options and 104,746 options respectively under the Company's Share Option Plan 2002. There have been no other changes in the directors' interests in the share capital between 31st December 2004 and the date of this report.

Details of share options held by the directors during the year were:

	Scheme (see below)	At 31st December 2003	Granted	Exercised	Lapsed	At 31st December 2004	Exercise price	Date from which exercisable	Expiry date
Stephen Booty	1	23,897	–	–	–	23,897	544p	Apr '05	Apr '12
	2	5,514	–	–	–	5,514	544p	Apr '05	Apr '12
	3	6,014	–	–	–	6,014	157.12p	Jun '06	Nov '06
	4	12,000	–	–	–	12,000	301p	Nov '06	Nov '13
	5	112,941	–	–	–	112,941	212.5p	Oct '05	Oct '12
Martyn Ellis	4	64,716	–	–	–	64,716	273.5p	Jun '06	Jun '13
William Holmes	1	43,137	–	–	–	43,137	510p	Oct '04	Oct '11
	2	5,882	–	–	–	5,882	510p	Oct '04	Oct '11
	3	10,453	–	–	–	10,453	157.12p	Jun '08	Nov '08
	4	58,823	–	–	–	58,823	212.5p	Oct '05	Oct '12
	4	12,000	–	–	–	12,000	301p	Nov '06	Nov '13
Justin Jewitt	1	45,883	–	–	–	45,883	425p	May '03	Note 5
	1	22,000	–	–	–	22,000	542.5p	Mar '04	Note 5
	2	7,058	–	–	–	7,058	425p	May '03	Note 5
	3	10,453	–	–	10,453	–	157.12p	Jun '08	Note 5
	4	12,000	–	–	–	12,000	301p	Nov '06	Note 5
Stephen Page	1	46,561	–	–	–	46,561	472.5p	Nov '03	Note 5
	2	6,349	–	–	–	6,349	472.5p	Nov '03	Note 5
	3	6,014	–	–	–	6,014	157.12p	Jun '06	Note 5
	4	75,294	–	–	–	75,294	212.5p	Oct '05	Note 5
	4	12,000	–	–	–	12,000	301p	Nov '06	Note 5
	5	75,294	–	–	–	75,294	212.5p	Oct '05	Note 5

Schemes:

1 Employee Share Option Scheme 1996 Options; performance target – EPS growth of RPI plus 5% per annum
2 Company Share Option Plan 1996 Options; performance target – EPS growth of RPI plus 5% per annum
3 SAYE Scheme Options
4 The 2002 Plan – "Normal Option"
5 The 2002 Plan – "Super Option"

Notes:

1 There is no cost to the employee for the receipt of options under the Employee Share Option Scheme 1996, Company Share Option Plan 1996 or the 2002 Plan. Deductions from earnings are made in respect of SAYE options.
2 Employee Share Option Scheme 1996, Company Share Option Plan 1996 and the 2002 Plan option prices are fixed at the mid-market price on the business day preceding the date of grant.
3 SAYE Scheme options are fixed at a discount of 20% from the average of the mid-market prices for the five business days immediately before the date of invitation.
4 The mid-market price at 31st December 2004 was 151 pence and the range during the year was 95.5 pence to 232 pence.
5 Subject to the discretion of the Remuneration Committee, following the termination of their employment, Justin Jewitt and Stephen Page may exercise all executive share options they currently hold in the period up to 27th May 2005 and 31st August 2005 respectively except the SAYE scheme options which lapsed on 27th November 2004 and 28th February 2005 respectively.
6 No options were exercised by directors in 2004.

On behalf of the Board

Sir Andrew Foster, Chairman, Remuneration Committee
7th March 2005

Corporate Governance

Introduction

The Company complied throughout the year with the provisions set out in the Combined Code published by the UK Financial Reporting Council in July 2003 ("the Code") except where indicated in this statement.

The manner in which the Group applies the principles of good governance contained in the Code is described in the appropriate parts of this annual report. Thus the application by the Company of the Code's principles to remuneration matters at pages 17 to 23 should be read in conjunction with the statement below.

The Board

The Board of directors leads and controls the Company by holding at least eight meetings a year at which its current and forecast performance are examined. Regular reports on monthly performance and other matters of importance to the Company ensure that the Board is supplied in a timely manner with the information necessary to make an informed judgement. In addition, the Board holds regular meetings to discuss and devise the Company's medium- and long-term strategic focus and management development strategy. Regular informal presentations are given and meetings held in order to advise directors of issues of importance affecting the Group.

In accordance with the provisions of its Articles of Association and with the Code, each director is subject to re-election by the Company's shareholders at the Annual General Meeting immediately following appointment and at least every three years thereafter.

The Board has a Schedule of Matters specifically reserved to it for decision and has approved the written terms of reference for the various committees to which it has delegated its authority in certain matters. The Schedule makes it clear that all directors have access to the advice and services of the Company Secretary and establishes a procedure for all directors to take independent advice, if necessary, at the Company's expense. Matters reserved to the Board include the recommendation or approval of dividends, the approval of final and interim financial statements, major financial commitments, the acquisition of companies or businesses, appointments to the Board and its committees, the Group's future strategy and the Group's internal controls. This Schedule is kept under regular review.

During the year, the Board was led by John Rennocks, the non-executive Chairman. He also served as a member of the Board's Audit, Remuneration and Nomination Committees.

The Chairman's responsibilities are clearly defined in a written specification agreed by the Board prior to his appointment in 2003. They include the smooth running of the Board, effective communication between executive and non-executive directors and the general progress and long-term development of the Group. His other significant commitments were disclosed to the Board prior to his appointment.

The day-to-day running of the Company's business is delegated to an executive team of three executive directors now led by Stephen Booty, who was appointed as the Group's Chief Executive in December 2004 and which also comprises Martyn Ellis, Finance Director and Dr William Holmes, who is responsible for the Group's clinical governance. Prior to May 2004, the executive team comprised four executive directors, led by Justin Jewitt and adopted a divisional structure. The changes to the structure of the executive element of the Board and the Group itself are more fully described in the Chairman's Statement.

During the year, three independent non-executive directors with extensive business, finance, health and social care backgrounds provided the Board with a breadth of experience and with independent judgement.

Roger Dye and Sir Andrew Foster were appointed as independent non-executive directors on 19th January 2004. Ingrid Alexander, CBE, served as an independent non-executive director throughout the year. Prior to his retirement on 19th January 2004, Robert Nicholls, CBE, served as an independent director and the Company's senior non-executive director. Sir Andrew Foster served as the Company's independent senior non-executive director from his appointment on the same date.

Having reviewed the Code, the Board considers that its present membership, comprising three independent non-executive directors, three executive directors and the Chairman, is appropriate, with a balance of skills and experience appropriate for the requirements of the business. This recognises that in John Rennocks, the Board has a Chairman who remains de facto "independent" (having met the criteria of independence referred to in Provision A 3.1. of the Code on his appointment in October 2003). It also considers that the Board's policies and procedures are of sufficient strength to ensure that the performance and proceedings of the Company are effectively challenged and controlled.

The Board actively encourages all directors to deepen their knowledge of their roles and responsibilities and to gain a clear understanding of the Company and the environment in which it operates. Newly appointed Board members undergo an induction programme and have received the opportunity to receive formal training. In 2004, the Group's non-executive directors received the opportunity to meet with various members of the Group's management teams. Further training for directors is available and offered as appropriate.

In 2004, the Board adopted a formal process for reviewing its own effectiveness and that of its individual members. In addition, it formalised its previously informal policy of holding regular meetings of the non-executive directors without the executive directors, and at least once a year, without the Chairman present, in order to evaluate his performance. The Board has undertaken interim reviews of its own effectiveness during the year, culminating in a formal review in January 2005. Assessments of individual directors were not considered by the Board to be appropriate during the year, taking into account the number of changes to the composition and structure of the Board and the issues affecting the Company during the year. However, the Board has agreed that such individual assessments will take place in 2005.

All non-executive directors meet the criteria of independence as laid down in Provision A 3.1. of the Revised Code with the exception of John Rennocks who met all of the criteria of independence on appointment and whom the Board currently regards de facto independent. For this reason, he remains a member of each of the Board's Nomination, Remuneration and Audit Committees. However, it intends to keep this under review.

Committees

The Board operates a number of committees, consisting wholly of non-executive directors to which it has delegated certain specific responsibilities and each of which has formally adopted terms of reference. These comprise the Nomination, Audit and Remuneration Committees.

Nomination Committee

The Nomination Committee, which makes recommendations to the Board on the appointment of directors, is chaired by John Rennocks. The Committee draws on the advice of the Group's Director of Human Resources and such professional advisors as it considers necessary. For the purposes of identifying the two non-executive directors appointed by the Board in January 2004, the Committee used the services of a firm of search consultants with particular expertise in the selection of non-executive directors. With the assistance of that firm of consultants and senior managers, the Committee drew up comprehensive specifications and undertook an extensive search before recommending candidates to the Board.

The Committee now comprises John Rennocks, Ingrid Alexander, Roger Dye and Sir Andrew Foster. Previously, Robert Nicholls and Justin Jewitt were also members of the Committee.

The Terms of Reference of the Nomination Committee are regularly reviewed by the Board.

The Nomination Committee was not called upon to make recommendations on the appointment of a Chief Executive following the resignation of Justin Jewitt. The Board considered it important to ensure the continuity of the Company's management at the time of significant change in the Company's business and believed that such continuity was best achieved by making an internal appointment with the result that Stephen Booty was appointed as Acting Chief Executive until his position as Chief Executive was confirmed by the Board in December 2004.

Audit Committee

The Audit Committee is chaired by Roger Dye, a chartered accountant and Finance Director of the Davis Service Group plc. It comprises only non-executive directors but includes John Rennocks as the Board is of the opinion that the Committee's work benefits from his financial expertise and experience gained as a former executive finance director and as Chairman of the Audit Committee of a number of other publicly listed companies. Mr Rennocks also acted as the Chairman of the Committee from 1st January 2004 until the appointment of Mr Dye as Chairman following the preliminary announcement of the Company's results for the year ended 31st December 2003, since of all of the non-executive directors serving on the Board at that time, he possessed the most recent and relevant financial experience and was most familiar with the Company's business during that year.

The other members of the Committee comprise Ingrid Alexander and Sir Andrew Foster and its Terms of Reference are regularly reviewed by the Board.

The Committee met four times during the year to review the preliminary and interim results before they were presented to the Board, to receive reports from the Company's internal and external auditors and to make recommendations to the Board on accounting policies. Its primary duties include the monitoring, on behalf of the Board, of compliance with and the effectiveness of the Company's accounting and internal control systems. The Committee's duties also include monitoring the scope and results of the Company's annual audit and the independence, general performance and objectivity of its auditors. The Committee has also agreed and implemented a procedure for reviewing and assessing its own effectiveness and that of the internal and external audit processes, including maintaining external auditor's objectivity and independence. The Chairman of the Committee also regularly meets informally with the auditors.

Corporate Governance continued

During the first three months of the year, the Company's internal audit function was outsourced to Deloitte & Touche, who reported regularly to the Audit Committee on projects undertaken in accordance with the audit plan agreed with the Committee at the beginning of every financial year. Copies of all reports issued by the internal auditors were circulated to all members of the Audit Committee as they were published. From April 2004, an in-house internal audit function were established, led by a Business Review Manager. The Business Review Team reports and is accountable to the Audit Committee in the same manner as was the outsourced function.

Remuneration Committee

The Remuneration Committee's responsibilities include determining the Group's overall remuneration strategy and the remuneration packages of the executive directors and other senior executives, after having consulted with the Chief Executive and having received professional advice from remuneration consultants and the Group's Director of Human Resources. The Committee is also responsible for approving the grant and exercise of executive long-term incentive arrangements. In determining remuneration policy, the Committee is free to obtain such professional advice as it sees fit, and regularly monitors both the policies of comparator companies and current market practice, in order to ensure that the packages provided are sufficient to attract and retain executive directors of the necessary quality.

The remuneration of non-executive directors, including the Chairman, is a matter for the Company's Board and the Committee's terms of reference make it clear that the framework for the remuneration of the Company's senior executives (including executive directors) must be agreed by the Board as a whole.

The terms of reference of the Committee are regularly reviewed by the Board.

The Committee met six times in the year.

From his appointment as a director on 19th January 2004, Sir Andrew Foster has acted as Chairman of the Remuneration Committee, which was previously chaired by Robert Nicholls, CBE, until his retirement from the Board on the same date.

The other members of the Committee are Ingrid Alexander, Roger Dye and John Rennocks, who is currently considered by the Board to be "de facto" independent and whose membership is therefore appropriate, although this is subject to ongoing review.

Short biographies of each of the directors, including their membership of the Board's committees outlined above, may be found on pages 12 and 13.

Attendance at Meetings

All directors attended those Board and Committee meetings to which they were entitled to attend, with the following exceptions:

Ms Alexander and Mr Holmes were each unable to attend one meeting of the Board, Sir Andrew Foster was unable to attend two meetings of the Audit Committee and John Rennocks was unable to attend one meeting of the Audit Committee. Mr Page did not attend one meeting of the Board that took place after the announcement of his resignation.

The Board, on the Company's behalf, recognises the need to maintain an active dialogue with its shareholders. The Chief Executive and Group Finance Director meet regularly with institutional investors and analysts to discuss the Company's performance and all shareholders have access to the senior non-executive director, who is available to discuss any questions which investors may have in relation to the running of the Company. They also have access to the Chairman of the Company if they so require. The Board encourages shareholders to attend the annual general meeting and is always willing to answer questions, either in the meeting itself or, more informally, afterwards. In addition, shareholders may contact the Company direct, either through its website or by telephoning its offices on 01707 255 635.

During the year, John Rennocks has contacted all of the Company's largest shareholders, offering to meet with them to discuss matters of strategy, corporate governance and any other issues that they wish to cover. He has met with the majority of these shareholders, some on a number of occasions, to discuss the Group's strategy in the light of the difficulties it has experienced during the year. The Company has also offered shareholders the opportunity to meet with the senior non-executive director if they so wish. However, no such meetings have taken place.

The Board also recognises the need to ensure that all directors are fully aware of the views of major shareholders about the Company. Copies of all analysts' research relating to the Company are circulated to all directors upon publication, quarterly analyses of the Company's shareholder register are made available to the Board and written feedback from shareholders and analysts, prepared by the Company's brokers and public relations advisors is provided to all directors after every significant corporate event and at least twice a year.

Going Concern

The directors confirm that, after reviewing the financial position and cash flows of the Group and of the Company, they have a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Internal Controls

As required by the UK Listing Authority, the Company has complied throughout the year with the provisions of the Code relating to internal controls, having implemented the procedures necessary to comply with the guidance issued in September 1999 (the Turnbull Committee Report) and to report in line with that guidance.

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

The directors first adopted a revised comprehensive process for managing, evaluating and reporting on significant risks faced by the Group in 1999. This process has been constantly reviewed and revised in subsequent years, including 2004. The revised (and further refined and extended) process has been in place for the whole of 2004 and up to the date of approval of the Annual Report and Accounts.

The key elements of the system operated by the Group to identify, evaluate and manage significant risks include the following:

- The Group's management operates a formal process for identifying, managing and reporting on operational, clinical and financial risks faced by each of the Group's businesses, whereby each of the risks identified is reviewed in detail by the executive directors on a semi-annual basis. Senior management team review meetings are held on at least a monthly basis at which the Group's business managers and executive team members report on the progress of the companies or discipline for which they are responsible and share best practice. The formal process for identifying discipline-specific risks across the Group's operations encompasses financial, IT, human resources, legal, property and clinical risks. A mechanism also exists to extend the Group's formal risk management processes to any significant new business acquired or begun by the Company immediately upon acquisition or start-up. In this way, the Board is able to confirm that the necessary process has been operated by the Group for the whole of 2004.

- At least twice a year, the Audit Committee of the Board reviews a register compiled by the managing director of each of the Group's businesses and registers compiled by certain members of the Group's senior management team, summarising the significant risks faced by the businesses or the Group as a whole, the likelihood of those risks occurring and the steps being taken to minimise or otherwise manage those risks.

- During the year, the Board has also refined its policies for managing the business risks it has identified as having the potential to impact significantly on the Group's performance. For example, in 2004, after the appointment of the Group's Business Review Team, it took steps better to align its risk management processes with the operational imperatives of the businesses by adopting a dynamic risk-management tool that assists the Group's operational management to identify developing trends at an early stage.

As required by the Turnbull Guidance, the Board has carried out an annual assessment of the effectiveness of the system of internal controls. The processes applied by the Board include:

- At the end of the year, the managing directors of each of the Group's businesses, including the Group's corporate resource, are required to complete and sign a register of the key financial and operational risks facing the business for which they are responsible and to confirm that they have complied throughout the year with the Company's policies and procedures on risk management. From these registers, a report identifying the key risks faced by the Group is compiled and signed by the Chief Executive, Group Finance Director and Group Company Secretary, who are also required to confirm their compliance with such procedures and policies. This report and the annual compliance statements of each of the managing directors, endorsed by the Divisional managing directors, are reviewed by the Board before the Annual Report and Accounts are approved.

- The Group has an independent Internal Audit function which reviews the overall effectiveness of the risk management process for the key risks and reports independently to the Audit Committee.

- At each meeting the Audit Committee reviews reports of the senior management team, internal and external auditors, on any issues identified as having a potentially substantial impact on the results of the Group, or areas of control weakness.

- The Audit Committee reviews the effectiveness of the Group's system of managing financial risk and refers any risks it considers significant to the Board for its consideration.

- At least twice a year, the Audit Committee reviews the work plans and results of each of the internal and external auditors.

- The Audit Committee Chairman reports the outcome of all Audit Committee meetings to the Board, which also receives minutes of all such meetings.

Auditors' Report

Report to the shareholders of Nestor Healthcare Group plc

Independent auditors' report to Nestor Healthcare Group plc

We have audited the financial statements which comprise the profit and loss account, the balance sheet, the cash flow statement, the statement of total recognised gains and losses and the related notes. We have also audited the disclosures required by Part 3 of Schedule 7A to the Companies Act 1985 contained in the directors' remuneration report ("the auditable part").

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities. The directors are also responsible for preparing the directors' remuneration report.

Our responsibility is to audit the financial statements and the auditable part of the directors' remuneration report in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the auditable part of the directors' remuneration report have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report, the unaudited part of the directors' remuneration report, the chairman's statement, the chief executive's review and financial review and the corporate governance statement.

We review whether the corporate governance statement reflects the Company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the auditable part of the directors' remuneration report. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the auditable part of the directors' remuneration report are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and the Group at 31st December 2004 and of the loss and cash flows of the Group for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- those parts of the directors' remuneration report required by Part 3 of Schedule 7A to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
1 Embankment Place
London WC2N 6RH
7th March 2005

Consolidated Profit and Loss Account

for the year ended 31st December 2004

	Notes	2004 Before goodwill amortisation and exceptional items £000	2004 Goodwill amortisation and exceptional items £000	2004 Total £000	2003 Before goodwill amortisation and exceptional items £000	2003 Goodwill amortisation and exceptional items £000	2003 Total £000
Turnover							
Existing		**385,488**	**–**	**385,488**	423,161	–	423,161
Acquisitions		**4,351**	**–**	**4,351**	–	–	–
Turnover	3	**389,839**	**–**	**389,839**	423,161	–	423,161
Cost of sales		**(291,361)**	**–**	**(291,361)**	(319,257)	–	(319,257)
Gross profit	3	**98,478**	**–**	**98,478**	103,904	–	103,904
Administrative expenses	3	**(77,835)**	**(8,841)**	**(86,676)**	(75,114)	(8,398)	(83,512)
Continuing operations							
Operating profit existing	3	**20,070**	**(8,724)**	**11,346**	28,790	(8,398)	20,392
Operating profit acquisitions	3	**573**	**(117)**	**456**	–	–	–
Operating profit	3,4	**20,643**	**(8,841)**	**11,802**	28,790	(8,398)	20,392
Exceptional items							
– loss on disposal of subsidiary undertaking	5	**–**	**(1,577)**	**(1,577)**	–	(2,680)	(2,680)
– fundamental restructuring cost	5	**–**	**(60,444)**	**(60,444)**	–	–	–
(Loss)/profit on ordinary activities before interest		**20,643**	**(70,862)**	**(50,219)**	28,790	(11,078)	17,712
Net interest payable	8	**(5,418)**	**–**	**(5,418)**	(4,110)	–	(4,110)
Profit on ordinary activities before taxation goodwill amortisation and exceptional items		**15,225**	**–**	**15,225**	24,680	–	24,680
Goodwill amortisation		**–**	**(8,841)**	**(8,841)**	–	(8,398)	(8,398)
Exceptional items		**–**	**(62,021)**	**(62,021)**	–	(2,680)	(2,680)
(Loss)/profit on ordinary activities before taxation		**15,225**	**(70,862)**	**(55,637)**	24,680	(11,078)	13,602
Tax on profit on ordinary activities	9	**(4,605)**	**2,170**	**(2,435)**	(4,353)	–	(4,353)
(Loss)/profit on ordinary activities after taxation		**10,620**	**(68,692)**	**(58,072)**	20,327	(11,078)	9,249
Equity minority interests		**(118)**	**–**	**(118)**	(47)	–	(47)
(Loss)/profit attributable to shareholders		**10,502**	**(68,692)**	**(58,190)**	20,280	(11,078)	9,202
Equity dividends	11	**(1,314)**	**–**	**(1,314)**	(8,427)	–	(8,427)
Retained (loss)/profit for the year	24	**9,188**	**(68,692)**	**(59,504)**	11,853	(11,078)	775
(Loss)/earnings per share							
Basic	12	**11.98p**	**(78.38p)**	**(66.40p)**	23.17p	(12.66p)	10.51p
Diluted	12	**11.98p**	**(78.38p)**	**(66.40p)**	23.05p	(12.59p)	10.46p
Adjusted for goodwill amortisation and exceptional items – basic	12	**11.98p**	**–**	**11.98p**	23.17p	–	23.17p
Adjusted for goodwill amortisation and exceptional items – diluted	12	**11.98p**	**–**	**11.98p**	23.05p	–	23.05p
Dividends per share	11	**1.50p**	**–**	**1.50p**	9.62p	–	9.62p

The historical cost (loss)/profit on ordinary activities before taxation and the historical cost (loss)/profit retained for the year after taxation and dividends are the same as those reported above.

Statement of Total Recognised Gains and Losses

for the year ended 31st December 2004

	Notes	2004 £000	2003 £000
(Loss)/profit attributable to shareholders		**(58,190)**	9,202
Total recognised (losses)/gains relating to the year		**(58,190)**	9,202
Prior year adjustment		**–**	463
Total (losses)/gains recognised since the last report		**(58,190)**	9,665

Reconciliation of Movements in Shareholders' Funds

for the year ended 31st December 2004

	Notes	2004 £000	2003 £000
(Loss)/profit attributable to shareholders		**(58,190)**	9,202
Dividends	11	**(1,314)**	(8,427)
Shares issued during the year		**2**	216
Net (decrease)/increase in shareholders' funds		**(59,502)**	991
Opening equity shareholders' funds as previously reported		**88,989**	87,535
Prior year adjustment		**–**	463
Opening equity shareholders' funds as restated		**88,989**	87,998
Closing equity shareholders' funds		**29,487**	88,989

Balance Sheets

as at 31st December 2004

	Notes	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Fixed assets					
Intangible assets	13	**106,767**	161,085	**–**	–
Tangible fixed assets	14	**7,534**	12,968	**23**	58
Investments	16	**–**	–	**113,487**	33,249
Total fixed assets		**114,301**	174,053	**113,510**	33,307
Current assets					
Debtors	17	**54,072**	61,496	**152,313**	465,145
Cash at bank and in hand		**979**	2,928	**114**	1,318
		55,051	64,424	**152,427**	466,463
Creditors – amounts falling due within one year	18	**(45,159)**	(52,172)	**(31,928)**	(48,145)
Net current assets		**9,892**	12,252	**120,499**	418,318
Total assets less current liabilities		**124,193**	186,305	**234,009**	451,625
Creditors – amounts falling due after more than one year	19	**(84,001)**	(90,004)	**(84,000)**	(90,000)
Provisions for liabilities and charges	22	**(10,655)**	(7,380)	**(386)**	(913)
Net assets		**29,537**	88,921	**149,623**	360,712
Capital and reserves					
Called up share capital	23	**8,763**	8,763	**8,763**	8,763
Share premium account	24	**43,224**	43,222	**43,224**	43,222
Other reserves	24	**864**	864	**25,750**	25,750
Profit and loss account	24	**(23,364)**	36,140	**71,886**	282,977
Equity shareholders' funds		**29,487**	88,989	**149,623**	360,712
Equity minority interests		**50**	(68)	**–**	–
		29,537	88,921	**149,623**	360,712

The notes on pages 33 to 53 form an integral part of these financial statements.

The financial statements on pages 29 to 53 were approved by the Board on 7th March 2005 and were signed on its behalf by:

J L Rennocks

M A Ellis

Consolidated Cash Flow Statement

for the year ended 31st December 2004

	2004 £000	2004 £000	2003 £000	2003 £000
Net cash inflow from operating activities before exceptional items (note 25)		**29,614**		24,990
Payments in respect of exceptional items		**(2,922)**		(1,899)
Returns on investments and servicing of finance				
Interest paid	**(5,620)**		(3,708)	
Interest received	**64**		50	
Dividends paid to minority interests	**–**		(71)	
Interest element of finance leases	**–**		(15)	
Net cash outflow from returns on investments and servicing of finance		**(5,556)**		(3,744)
Taxation		**(3,930)**		(5,711)
Net cash inflow before investing activities and equity dividends paid		**17,206**		13,636
Capital expenditure and financial investment				
Purchase of tangible fixed assets (note 14)	**(2,823)**		(9,948)	
Sale of tangible fixed assets	**280**		4,218	
Net cash outflow from capital expenditure and financial investment		**(2,543)**		(5,730)
Acquisitions and disposals				
Purchase of businesses and subsidiary undertakings (note 16)	**(4,930)**		(31,108)	
Net cash acquired with subsidiary undertakings (note 16)	**368**		1,563	
Deferred consideration received from sale of business	**–**		260	
Net cash outflow from acquisitions and disposals		**(4,562)**		(29,285)
Equity dividends paid		**(5,381)**		(8,420)
Net cash inflow/(outflow) before financing		**4,720**		(29,799)
Financing				
Issue of ordinary share capital	**2**		216	
Capital element of finance lease payments (note 25)	**(14)**		(479)	
(Decrease)/increase in borrowing	**(7,407)**		25,708	
Net cash (outflow)/inflow from financing		**(7,419)**		25,445
Decrease in net cash		**(2,699)**		(4,354)

The notes to the Consolidated Cash Flow Statement are shown in note 25 to the financial statements.

The post acquisition trading of the businesses acquired during the year generated operating profit before goodwill amortisation of £0.6 million. It is not practicable to determine the impact of acquisitions on other cash flow items.

Notes to the Financial Statements

for the year ended 31st December 2004

1 Accounting policies

Presentation of statement of profit and loss

A columnar presentation has been adopted in the statement of profit and loss in order to illustrate underlying business performance as this is the primary measure used by management. For this purpose, goodwill amortisation, goodwill impairment and other exceptional items are excluded from business performance.

Basis of accounting

The financial statements have been prepared in accordance with applicable accounting standards and the Companies Act 1985 under the historical cost convention.

Basis of consolidation

The results of businesses acquired are included from the effective date of acquisition and businesses sold are included up to the date of disposal.

The accounting reference date of the Company and all its trading subsidiary undertakings is 31st December.

Turnover

Revenue is recognised in the profit and loss account when goods or services are supplied to external customers against orders received.

Goodwill and amortisation

Purchased goodwill, being the excess of the purchase consideration over the fair value of the net assets of newly acquired undertakings, is capitalised on the balance sheet, and amortised over its useful economic life not exceeding 20 years. Prior to 1st January 1998, all purchased goodwill was written off to reserves on acquisition. Previously written off goodwill has not been reinstated and is charged to the profit and loss account on the disposal or termination of the related business.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less depreciation and impairment. Depreciation is calculated so as to write down the cost of tangible assets to their estimated residual value in equal instalments over their estimated useful lives. The range of estimated useful lives for each major asset category, which are reviewed annually, are:

Leasehold land and buildings	Term of the lease
Plant and equipment, fixtures and fittings (including computer equipment)	3 to 8 years

Fixed asset investments

Investments in subsidiary undertakings are held at original cost less any provision for impairment.

Corporation tax

The amount included in the profit and loss account is based on pre-tax reported income/losses and is calculated at current tax rates, taking into account timing differences and the likelihood of realisation of deferred tax assets and liabilities.

Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Group's taxable profits and its results as stated in the financial statements. An asset is not recognised to the extent that the transfer of economic benefits in the future is uncertain.

Deferred tax is measured at the tax rate expected to apply in the periods in which the timing differences are expected to reverse based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

Pension costs

Pension costs are charged to the profit and loss account in such a way as to provide for the liabilities evenly over the average remaining working lives of the employees. Any difference between this charge and contributions paid based on actuarial assumptions is included as an asset or liability in the consolidated balance sheet. The Group has adopted the transitional rules on actuarially determined pensions disclosure as prescribed by FRS 17.

Leases

Where fixed assets are financed by leasing agreements which give rights approximately equivalent to ownership (finance lease), the assets are capitalised and depreciated accordingly on a straight line basis over the life of the lease. The corresponding lease commitments are treated as obligations to the lessor. All other lease payments are charged to the profit and loss account in the year to which they relate.

Notes to the Financial Statements
for the year ended 31st December 2004

1 Accounting policies continued

Derivative financial instruments
The Group enters into derivative instruments primarily to manage exposures to fluctuations in interest rates. Interest differentials under interest rate collar instruments are recognised on an accruals basis.

Foreign currency
Assets and liabilities denominated in foreign currencies are translated into sterling at the financial year end exchange rates.

2 International Financial Reporting Standards (IFRS)

In June 2002, the Council of the European Union adopted a Regulation requiring listed companies in its Member States to prepare their consolidated financial statements in accordance with International Accounting Standards from 2005. The Group's first financial results announcement prepared in accordance with IFRS will be that for the first half of 2005, and the first Annual Report prepared under IFRS will be that for the year ending 31st December 2005. The Group's project to convert its financial reporting from UK GAAP to IFRS is underway. Restated summary financial statements for the year ended 31st December 2004 (without comparatives for the year ended 31st December 2003) will be prepared ahead of the results announcement for the first half of 2005.

3 Segmental reporting

Following a reorganisation of the Group in 2004, operations are now conducted and managed through three segments – Healthcare Staffing, Social Care and Primary Care. Segmental results are reported on this basis and comparatives restated. Costs have been allocated on a specific basis where possible, and certain central costs on a reasonable and consistent basis.

The UK was the origin and destination of all of the Group's turnover in both 2004 and 2003. All turnover is derived from external customers.

	2004 £000	2003* £000
Turnover by business activity		
Healthcare Staffing	**166,001**	210,040
Social Care	**103,514**	89,259
Primary Care	**120,324**	123,862
Total	**389,839**	423,161

* As restated

	Total operating profit/(loss) before goodwill amortisation and exceptional items		Total operating profit/(loss)	
	2004 £000	2003* £000	**2004 £000**	2003* £000
Operating profit/(loss) by business activity				
Healthcare Staffing	**8,074**	18,610	**6,039**	17,001
Social Care	**12,725**	9,985	**9,836**	8,313
Primary Care	**(156)**	195	**(4,073)**	(4,922)
Total	**20,643**	28,790	**11,802**	20,392

* As restated

Central costs have been allocated across the business segments on the basis of activity and on a consistent basis.

3 Segmental reporting continued

Turnover, cost of sales, gross profit, administrative expenses and operating profit are analysed between existing and acquired operations as follows:

	Continuing existing 2004 £000	Continuing acquisitions 2004 £000	Total 2004 £000	Total 2003 £000
Turnover	**385,488**	**4,351**	**389,839**	423,161
Cost of sales	**(288,285)**	**(3,076)**	**(291,361)**	(319,257)
Gross profit	**97,203**	**1,275**	**98,478**	103,904
Administrative expenses – ongoing	**(77,133)**	**(702)**	**(77,835)**	(75,114)
– goodwill amortisation	**(8,724)**	**(117)**	**(8,841)**	(8,398)
Total administrative expenses	**(85,857)**	**(819)**	**(86,676)**	(83,512)
Operating profit	**11,346**	**456**	**11,802**	20,392

The contribution from acquisitions shown above and on the face of the profit and loss account reflects the contribution from businesses that were acquired during the year.

	Net operating assets 2004 £000	2003* £000
Analysis of net operating assets by business activity		
Healthcare Staffing	**40,206**	46,188
Social Care	**38,625**	40,001
Primary Care	**33,162**	88,439
Central	**2,166**	3,637
Total continuing operations	**114,159**	178,265

* As restated

	2004 £000	2003 £000
Net assets per consolidated balance sheet	**29,537**	88,921
Net debt	**84,622**	89,344
Total net operating assets, including goodwill	**114,159**	178,265

All material operating assets were held in the United Kingdom in both 2004 and 2003.

4 Operating profit

	2004 £000	2003 £000
Operating profit is stated after charging/(crediting)		
Depreciation	**4,636**	5,418
Amortisation of goodwill	**8,841***	8,398
Net (profit)/loss on sale of tangible fixed assets	**(128)**	331
Auditors' remuneration – statutory audit	**387**	410
Operating lease rentals:		
Land and buildings	**4,732**	4,859
Plant and machinery	**1,482**	172

* Amortisation of goodwill includes £496,000 impairment of the carrying value of goodwill arising on acquisitions made in 2003.

Remuneration of the Company's auditors in respect of other services amounted to £302,000 (2003: £280,000). This comprises £224,000 for tax compliance services, £50,000 for further assurance services and £28,000 for structuring services.

Auditors' remuneration includes £40,000 (2003: £40,000) relating to the Company.

5 Exceptional items

Exceptional items charged to the profit and loss account comprise:

	2004 £000	2003 £000
Impairment of goodwill	**48,613**	–
Asset impairments and write offs	**4,844**	–
Onerous property lease costs	**4,903**	–
Severance and other reorganisation costs	**2,084**	–
Settlement of tax liability relating to a discontinued operation	**1,577**	–
Loss on disposal of business	**–**	2,680
	62,021	2,680

The impairment of goodwill relates to the carrying value of goodwill arising from the purchase of the Healthcall group of companies in 2001. Following a deterioration in prospects for parts of this business, the Board has undertaken a detailed reforecasting exercise, the discounted cash flows of which form the basis of the valuation of goodwill. The result of this exercise, using the Group's cost of capital, reduces the carrying value of the Healthcall goodwill at the year end by £48,613,000.

During the year, the Group underwent a fundamental reorganisation of its business activity, incurring the following exceptional costs:

(a) Asset impairments and write offs of £4,844,000 relate to the value of assets written down or written off when the Group has ceased operations, and ceased occupancy, in certain locations.
(b) Onerous lease costs identified following the closure of the Sheffield Clinical Response Centre and the rationalisation of the branch network across all business activities. A charge of £4,903,000 has been made, taking into account estimates of the length of time properties will be vacant (net of any potential sub-lease income where this can be estimated with a high degree of probability) together with any dilapidation costs and other costs associated with the termination or disposal of leases.
(c) Severance and other reorganisation costs amounting to £2,084,000 primarily relate to amounts paid or payable to employees whose redundancies had been initiated by 31st December 2004.

The settlement of a tax liability relating to a discontinued operation, amounting to £1,577,000, relates to the sale of the Group's U.S. staffing business Cross Country Staffing ("CCS") in 1999. The Internal Revenue Service of the U.S. issued a payroll tax assessment against CCS and its partners in 1998 amounting to $21.8 million. In February 2004, CCS and its partners submitted a written offer to the US Department of Justice proposing to settle all claims for a cash sum of $13.0 million, the Group's share of which would be $2.9 million. The Group has recently received advice that the U.S. authorities are likely to accept this settlement offer. The Group has accordingly considered it appropriate to take an exceptional charge of $3.125 million (including estimated legal costs), equivalent to £1,577,000 at the U.S. dollar exchange rate of $1.87 used. It is expected that this settlement sum will be confirmed and paid during the course of 2005.

A tax credit of £2,170,000 has been recognised in respect of all the exceptional charges made in the year.

The exceptional item charged in 2003 on disposal of a discontinued operation of £2,680,000 comprises the loss on disposal of the Healthcall Optical business that formed part of the Services Division. At 31st December 2003, the Board had resolved to dispose of this business; and the disposal was completed in 2004. No tax credit has been recognised in respect of this exceptional loss.

6 Employees

	2004 £000	2003 £000
Employee costs		
Wages and salaries	**56,744**	56,425
Social security costs	**5,023**	4,920
Other pension costs	**1,969**	2,364
	63,736	63,709

6 Employees continued

	2004	2003
Average number of persons employed		
Full-time	**2,088**	2,001
Part-time	**1,574**	2,880
	3,662	4,881

	2004	2003*
Employee numbers by business activity		
Healthcare Staffing	**831**	1,232
Social Care	**729**	979
Primary Care	**2,102**	2,670
	3,662	4,881

* As restated

7 Directors' emoluments

	2004 £000	2003 £000
Aggregate emoluments	**2,047**	1,642
Company contributions to money purchase pension schemes	**52**	79
	2,099	1,721

Aggregate emoluments include £574,000 (2003: £217,000) compensation for loss of office, including £75,000 (2003: £Nil) company contributions to money purchase pension schemes.

The detailed numerical analysis of directors' remuneration is included in the tables in the Remuneration Report on pages 17 to 23 and forms part of these financial statements.

8 Net interest payable

	2004 £000	2003 £000
Unwinding of discount in provisions (note 22)	**(337)**	(384)
Amortisation of issue costs of bank loan	**(33)**	(33)
Interest payable on bank loans and overdrafts	**(5,085)**	(3,697)
Interest payable on other loans	**(27)**	(31)
Interest payable on finance leases	**-**	(15)
Total interest and similar charges payable	**(5,482)**	(4,160)
Bank interest receivable	**64**	50
Net interest payable	**(5,418)**	(4,110)

9 Taxation

	2004 £000	2003 £000
UK Corporation Tax at 30.00% (2003 – 30.00%) on taxable profits for the year	**(2,479)**	(6,010)
Over provision in previous years	**103**	1,678
Current tax	**(2,376)**	(4,332)
Deferred tax	**(59)**	(21)
Tax on profit on ordinary activities	**(2,435)**	(4,353)

Notes to the Financial Statements

for the year ended 31st December 2004

9 Taxation continued

The effective tax rate for the year is higher than the standard rate of corporation tax for the UK. The differences are explained below:

	2004 £000	2003 £000
Loss/(profit) on ordinary activities at the standard rate of corporation tax at 30%	**16,691**	(4,081)
Exceptional charges not deductible	**(16,436)**	–
Other items not deductible	**(123)**	(199)
Net goodwill amortisation and impairment not deductible	**(2,652)**	(1,790)
Timing differences	**41**	100
Losses not relievable	**–**	(40)
Over provision in previous years	**103**	1,678
Current tax charge for the year	**(2,376)**	(4,332)

The effective tax rate for future years is expected to approximate to 30%.

10 (Loss)/profit for the year

The loss after tax for the year dealt with in the accounts of the Company amounts to £209,777,000 (2003: profit of £15,947,000) reflecting the impact of certain transactions with other Group companies that formed part of an internal reorganisation of the Group structure. As allowed by the provisions of Section 230 of the Companies Act 1985, the Company has not published its own profit and loss account.

11 Dividends

	2004 £000	2003 £000
Equity dividends paid Ordinary shares: nil per share (2003 – 3.48p)	**–**	3,046
Equity dividends proposed Ordinary shares: 1.50p per share (2003 – 6.14p)	**1,314**	5,381
Total dividends: 1.50p per share (2003 – 9.62p)	**1,314**	8,427

12 Earnings per share

Basic (loss)/earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The Group has only one category of potentially dilutive potential ordinary shares: those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the year. In the year to 31st December 2004 there were no such options, as the exercise price of all outstanding options was higher than the average market price. Diluted earnings per share is accordingly identical to basic earnings per share.

12 Earnings per share continued

Reconciliations of the earnings and weighted average number of shares used in the calculations are set out below.

	2004 Earnings £000	2004 Weighted average number of shares thousand	2004 EPS pence	2003 Earnings £000	2003 Weighted average number of shares thousand	2003 EPS pence
Basic (loss)/earnings per share	**(58,190)**	**87,633**	**(66.40p)**	9,202	87,545	10.51p
Dilutive effect of options	–	–	–	–	439	(0.05p)
Diluted (loss)/earnings per share	**(58,190)**	**87,633**	**(66.40p)**	9,202	87,984	10.46p
Adjusted to exclude goodwill amortisation and exceptional items						
Basic (loss)/earnings per share	**(58,190)**	**87,633**	**(66.40p)**	9,202	87,545	10.51p
Exceptional items (adjusted for taxation)	**59,851**	–	**68.30p**	2,680	–	3.06p
Goodwill amortisation	**8,841**	–	**10.08p**	8,398	–	9.60p
Adjusted basic earnings per share	**10,502**	**87,633**	**11.98p**	20,280	87,545	23.17p
Diluted (loss)/earnings per share	**(58,190)**	**87,633**	**(66.40p)**	9,202	87,984	10.46p
Exceptional items (adjusted for taxation)	**59,851**	–	**68.30p**	2,680	–	3.05p
Goodwill amortisation	**8,841**	–	**10.08p**	8,398	–	9.54p
Adjusted diluted earnings per share	**10,502**	**87,633**	**11.98p**	20,280	87,984	23.05p

13 Intangible assets

	Goodwill £000
Group	
Cost	
At 1st January 2004	185,427
Additions (note 16)	3,136
At 31st December 2004	188,563
Aggregate amortisation	
At 1st January 2004	24,342
Charge for the year	8,841
Exceptional impairment	48,613
At 31st December 2004	81,796
Net book value	
At 31st December 2004	106,767
At 31st December 2003	161,085

The goodwill arising on all acquisitions is being amortised on a straight-line basis over 20 years. This is the period over which the directors estimate that the value of the underlying businesses acquired is expected to exceed the value of the underlying assets.

In 2004, the directors have evaluated the carrying values of goodwill. As a result, the carrying value of the goodwill relating to the Healthcall Group business has been impaired by £48,613,000. This impairment has been taken as an exceptional charge.

In addition, the directors have specifically evaluated the carrying values of goodwill for all acquisitions of businesses and subsidiary undertakings made in 2003. As a result, the carrying value of the goodwill relating to two of those acquisitions has been impaired by £496,000. This impairment has been included with the charge for amortisation for the year in the table above.

Evaluations of the carrying value of goodwill have been performed by discounting projected future cash flows using a pre-tax nominal discount rate equivalent to the estimated weighted average cost of capital currently applicable to the Group.

14 Tangible fixed assets

	Leasehold land & buildings £000	Plant & equipment, fixtures & fittings £000	Total £000
Group			
Cost			
At 1st January 2004	82	23,880	23,962
Additions	–	2,823	2,823
On acquisition of businesses and subsidiary undertakings	–	37	37
Disposals	–	(13,231)	(13,231)
At 31st December 2004	82	13,509	13,591
Depreciation			
At 1st January 2004	46	10,948	10,994
Disposals	–	(9,573)	(9,573)
Charge for the year	10	4,626	4,636
At 31st December 2004	56	6,001	6,057
Net book value			
At 31st December 2004	26	7,508	7,534
At 31st December 2003	36	12,932	12,968

Disposals include amounts eliminated on the write off of assets when the Group has ceased operations, and ceased occupancy, in certain locations.

At 31st December 2004, the net book value of assets held under finance leases, capitalised and included in plant and equipment, fixtures and fittings amounts to £nil (2003: £14,000). The depreciation charge on these assets during the year amounted to £10,000 (2003: £231,000).

	Plant & equipment, fixtures & fittings £000
Company	
Cost	
At 1st January 2004	287
Additions	4
Disposals	–
At 31st December 2004	291
Depreciation	
At 1st January 2004	229
Disposals	–
Charge for the year	39
At 31st December 2004	268
Net book value	
At 31st December 2004	23
At 31st December 2003	58

15 Capital commitments

	2004 £000	2003 £000
Capital expenditure that has been contracted but not provided for	–	135

16 Fixed asset investments

	Investment in subsidiaries £000
Company	
At 1st January 2004	33,249
Impairments	(33,249)
Additions	113,487
At 31st December 2004	113,487

Impairments relate to the impact of certain transactions with, and assessment of carrying values of investments in, other Group companies that formed part of an internal reorganisation of the Group structure. Additions relate primarily to the capitalisation of a newly formed intermediate holding company, Helenus Limited, as part of the same internal reorganisation of the Group structure.

Except where stated, the following subsidiary companies are wholly-owned, including 100% voting rights, operate in the United Kingdom and are registered in England & Wales. All companies have been included in the consolidated results of the Group.

Principal undertakings

Undertaking	Business
Nestor Primecare Services Limited [1]	UK healthcare services and flexible staffing services in UK health and social care
Care Monitoring 2000 Limited [2]	Homecare remote monitoring
Holt Medical Recruitment Limited [1]	Flexible staffing in UK healthcare
Prime Care Services Limited [1]	Provision of social care services
Nestor Equipment Leasing Limited [1]	Provision of asset leasing
Helenus Limited	Intermediate holding company

[1] The interest of Nestor Healthcare Group plc is held through intermediate holding companies.
[2] Nestor Healthcare Group plc has a 51% interest.

Related party transactions

Neither the Group nor the Company had any material transactions with related parties during the year. Details of transactions with directors are set out in the Remuneration Report on pages 17 to 23.

Business acquisitions

During the year, the group purchased four companies and one business for a total consideration of £2,920,000, plus capitalised costs of acquisition amounting to £177,000. All of these purchases have been accounted for as acquisitions.

In addition, adjustments were made to reduce the total consideration for acquisitions made in 2003 by £901,000, reflecting the finalisation of contingent consideration payable under the various purchase agreements. Adjustments to goodwill arising on these same acquisitions reflected both the reduction in total consideration and also the finalisation of net assets acquired following detailed review. Further capitalised costs amounting to £234,000 relating to the same 2003 acquisitions were incurred.

The two more significant acquisitions made in 2004 were of Care Initiative Limited ("Care Initiative") and Highfield Home Care Limited ("Highfield"), both acquired in February. The remaining acquisitions have not been separately analysed as individually their contribution to goodwill is not material.

The provisional fair values of assets and liabilities acquired in the year, which represent their book values, and adjustments thereof relating to the 2003 acquisitions, and the goodwill arising are outlined in the table below. All values of assets, liabilities and goodwill arising on the 2004 acquisitions will be finalised in the 2005 financial statements when detailed reviews of businesses acquired are completed. The payment of deferred consideration will be dependent on future performance of the businesses acquired.

Notes to the Financial Statements
for the year ended 31st December 2004

16 Fixed asset investments continued

	2004 acquisitions Care Initiative £000	2004 acquisitions Highfield £000	Other £000	Adjustments re 2003 acquisitions £000	Total £000
Fixed assets	16	6	7	8	37
Current assets and liabilities					
Debtors and prepayments	25	244	139	(1,083)	(675)
Creditors and accruals	(185)	(117)	(122)	(10)	(434)
Net cash	135	58	72	103	368
Net current assets	(25)	185	89	(990)	(741)
Creditors – amounts falling due after more than one year	–	(1)	(1)	–	(2)
Net assets acquired	(9)	190	95	(982)	(706)
Purchase consideration	847	1,022	1,051	(901)	2,019
Costs of acquisition	55	50	72	234	411
Total cost	902	1,072	1,123	(667)	2,430
Total goodwill arising in year (note 13)	911	882	1,028	315	3,136

Cash flows in respect of purchase of businesses

	Total £000
2004 acquisitions:	
Total consideration	2,920
Costs of acquisition	177
	3,097
Less: deferred and retained consideration accrued, not yet paid	(230)
	2,867
Less: net cash acquired	(368)
	2,499
2003 acquisitions:	
Deferred and retained consideration previously accrued, paid in 2004	2,063
Total net cash flows in respect of purchase of businesses	4,562

From the dates of acquisition to 31st December 2004, acquired businesses contributed £4,351,000 to turnover (including Care Initiative – £1,303,000, Highfield – £1,703,000) and £573,000 to profit before interest, goodwill amortisation and exceptional items (including Care Initiative – £276,000, Highfield £193,000).

In the year ended 31st March 2003, the last full financial year prior to acquisition, Care Initiative reported profit after tax of £165,000. For the period 1st April 2003 to 27th February 2004, Care Initiative reported profit after tax of £137,000.

In the year ended 31st August 2003, the last full financial year prior to acquisition, Highfield reported profit after tax of £77,000. For the period 1st September 2003 to 27th February 2004, Highfield reported profit after tax of £58,000.

17 Debtors

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Trade debtors	**43,050**	41,835	–	–
Amounts owed by Group companies	–	–	**126,753**	442,329
Dividends receivable from Group companies	–	–	**25,000**	22,000
Other debtors	**3,383**	1,734	**444**	618
Deferred tax receivable within one year	**157**	450	–	5
Prepayments and accrued income	**4,495**	14,699	**116**	193
Debtors receivable within one year	**51,085**	58,718	**152,313**	465,145
Deferred tax receivable after more than one year	**2,987**	2,778	–	–
Total debtors	**54,072**	61,496	**152,313**	465,145

Deferred tax

At 31st December 2004, the Group has an overall deferred tax asset from the recognition of a pension liability and from the deferral of claims for capital allowances. The deferred tax asset is shown as part of debtors. No recognition has been given to the carry forward of certain losses available for future tax relief as their recovery is not considered certain. The deferred tax asset is as follows:

	2004 £000	2003 £000
Pension liability	**1,247**	1,331
Accelerated capital allowances	**1,818**	1,618
Losses	**255**	291
Other	**79**	243
Total potential deferred tax asset	**3,399**	3,483
Less: losses not relievable	**(255)**	(255)
Total recognised deferred tax asset	**3,144**	3,228

18 Creditors – amounts falling due within one year

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Bank overdraft and loans (note 20)	**1,601**	851	**7,116**	19,837
Loan other than from banks	–	1,407	–	1,407
Finance leases	–	14	–	–
Trade creditors	**12,735**	8,102	–	–
Amounts owed to Group companies	–	–	**20,200**	19,876
Dividends proposed (note 11)	**1,314**	5,381	**1,314**	5,381
Corporation tax	**2,216**	3,495	–	–
Other tax and social security	**4,364**	5,899	–	–
Other creditors	**10,383**	10,227	**777**	982
Accruals and deferred income	**12,546**	16,796	**2,521**	662
	45,159	52,172	**31,928**	48,145

19 Creditors – amounts falling due after more than one year

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Bank loan	**84,000**	90,000	**84,000**	90,000
Other creditors	**1**	4	–	–
	84,001	90,004	**84,000**	90,000

Notes to the Financial Statements

for the year ended 31st December 2004

20 Net borrowings

	Interest rates	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Unsecured					
Bank overdraft and loans	variable	**(85,601)**	(90,851)	**(91,116)**	(109,837)
Loan other than from banks	variable	–	(1,407)	–	(1,407)
Finance leases		–	(14)	–	–
Total borrowings		**(85,601)**	(92,272)	**(91,116)**	(111,244)
Cash at bank and in hand		**979**	2,928	**114**	1,318
Net borrowings		**(84,622)**	(89,344)	**(91,002)**	(109,926)

Net borrowings for the Group are summarised as follows

	Repayable within 1 year £000	Repayable between 1 and 2 years £000	Repayable between 2 and 5 years £000	Total £000
Unsecured:				
Bank overdraft and loans	(1,601)	(84,000)	–	(85,601)
Total borrowings	(1,601)	(84,000)	–	(85,601)
Cash at bank and in hand	979	–	–	979
At 31st December 2004	(622)	(84,000)	–	(84,622)
At 31st December 2003	656	–	(90,000)	(89,344)

Net borrowings for the Company are summarised as follows

	Repayable within 1 year £000	Repayable between 1 and 2 years £000	Repayable between 2 and 5 years £000	Total £000
Unsecured:				
Bank overdraft and loans	(7,116)	(84,000)	–	(91,116)
Total borrowings	(7,116)	(84,000)	–	(91,116)
Cash at bank and in hand	114	–	–	114
At 31st December 2004	(7,002)	(84,000)	–	(91,002)
At 31st December 2003	(19,926)	–	(90,000)	(109,926)

21 Financial Instruments

An explanation of the role that financial instruments have had during the year in creating or changing the risks that the Group faces in its activities is set out in the Financial Review on page 8. Short term debtors and creditors have been excluded from all the following disclosures.

Interest rate profile of financial liabilities

The interest rate profile of the Group's financial liabilities at 31st December 2004 was:

	Floating rate financial liabilities £000	Financial liabilities on which no interest paid £000	Total £000
At 31st December 2004 – all sterling	92,098	1	92,099
At 31st December 2003 – all sterling	95,216	4	95,220

21 Financial Instruments continued

All the Group's creditors falling due within one year (other than bank and other borrowings) are excluded from the above tables either due to their short-term nature or because they do not meet the definition of a financial liability, such as tax balances.

Included in floating rate liabilities are £35,000,000 of borrowings upon which the Group has entered into interest rate swaps that have the effect of restricting LIBOR rates on those borrowings to between 4.0% and 5.6%. The net fair value of these swaps at 31st December 2004 was £nil.

Included in the above are the Group's provisions of £6,497,000 (2003: £2,944,000) for onerous contracts and other property provisions (note 22) which meet the definition of financial liabilities. These financial liabilities are considered to be floating rate liabilities as, in establishing the provisions, the cash flows have been discounted and the discount rate is re-appraised at each half yearly reporting date to ensure that it reflects current market assessments of the time value of money and the risks specific to the liability. Other floating rate financial liabilities bear interest at rates, based on LIBOR, which are fixed in advance for periods of between one month and six months.

The weighted average period to maturity of financial liabilities that bear no interest at 31st December 2004 was 1.5 years (2003 – 1.5 years).

Interest rate profile of financial assets

The interest rate profile of the Group's financial assets was:

Currency	Floating rate financial assets £000	Financial assets on which no interest received £000	Total £000
Sterling	933	22	955
Australian dollars	–	17	17
New Zealand dollars	–	7	7
At 31st December 2004	933	46	979
Sterling	2,878	13	2,891
Australian dollars	–	23	23
New Zealand dollars	–	14	14
At 31st December 2003	2,878	50	2,928

The financial assets comprise loan notes, bank deposits, bank current account balances and cash in hand. The floating rate financial assets earn interest at rates based on relevant national LIBOR equivalents and are all recoverable within one year or on demand. The financial assets on which no interest is received are balances on bank current accounts and cash in hand.

Maturity of financial liabilities

The maturity profile of the Group's financial liabilities at 31st December 2004 was:

	Debts £000	Other financial liabilities £000	Total £000
Within 1 year, or on demand	1,601	2,465	4,066
Between 1 and 2 years	84,000	1,912	85,912
Between 2 and 5 years	–	1,415	1,415
Over 5 years	–	706	706
At 31st December 2004	85,601	6,498	92,099

21 Financial Instruments continued

Maturity of financial liabilities continued

	Debts £000	Other financial liabilities £000	Total £000
Within 1 year, or on demand	2,272	904	3,176
Between 1 and 2 years	–	281	281
Between 2 and 5 years	90,000	886	90,886
Over 5 years	–	877	877
At 31st December 2003	92,272	2,948	95,220

Other financial liabilities include the provision for onerous contracts and other property provisions totalling £6,497,000 (2003: £2,944,000).

Borrowing facilities

The Group had the following undrawn floating rate committed borrowing facilities available in respect of which all conditions precedent had been met at that date:

	2004 £000	2003 £000
Expiring within 1 year	–	–
Expiring between 1 and 2 years	16,000	–
Expiring in more than 2 years	–	3,593
	16,000	3,593

All the above facilities incur commitment fees at market rates.

Fair values of financial assets and financial liabilities

The following table shows a comparison between the carrying amounts and the fair values of the Group's financial assets and financial liabilities. Fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties, other than a forced or liquidation sale and excludes accrued interest. For floating rate financial assets and liabilities, fair values approximate to book values.

	2004		2003	
	Book value £000	**Fair value £000**	Book value £000	Fair value £000
Financial assets	**979**	**979**	2,928	2,928
Short-term financial liabilities	**(1,601)**	**(1,601)**	(2,272)	(2,272)
Long-term borrowings	**(84,000)**	**(84,000)**	(90,000)	(90,000)
Other financial liabilities	**(6,498)**	**(6,498)**	(2,948)	(2,948)
	(91,120)	**(91,120)**	(92,292)	(92,292)

22 Provisions for liabilities and charges

	Pensions £000	Property £000	Total £000
Group			
At 1st January 2004	4,436	2,944	7,380
Transfer to profit and loss account	–	(51)	(51)
Exceptional charge	–	3,927	3,927
Utilised in the year	(500)	(438)	(938)
Unwinding of discount	222	115	337
At 31st December 2004	4,158	6,497	10,655
Company			
At 1st January 2004	–	913	913
Transfer to profit and loss account	–	(296)	(296)
Utilised in the year	–	(264)	(264)
Unwinding of discount	–	33	33
At 31st December 2004	–	386	386

Pensions

Following the acquisition of Healthcall in 2001 and as part of the process for finalising the provisional fair value of the assets and liabilities acquired, an actuarial deficit on the Healthcall pension fund was recognised on a discounted basis using appropriate government bond rates.

Property

The Group property provision of £6,497,000 (2003: £2,944,000) comprises £4,636,000 (2003: £2,383,000) in respect of lease contracts for properties no longer occupied by the Group, £731,000 (2003: £Nil) in respect of associated lease dilapidations, £381,000 (2003: £119,000) in respect of associated other exit costs, and £749,000 (2003: £442,000) in respect of lease dilapidation obligations relating to properties that continue to be occupied.

The Company property provision of £386,000 comprises £386,000 (2003: £913,000) in respect of lease contracts for properties no longer occupied by the Company.

The Group has a number of properties that are either vacant or underlet at a discount.
Provision has been made for onerous lease costs taking into account estimates of the length of time properties will be vacant (net of any potential sub-lease income where this can be estimated with a high degree of probability), together with any dilapidation costs and other costs associated with the termination or disposal of leases. In determining the provision for vacant properties, the cash flows have been discounted using appropriate government bond rates.

23 Share capital

	Authorised		Allotted, issued and fully paid	
	Number	£000	Number	£000
Ordinary shares of 10p each				
At 1st January 2004	96,000,000	9,600	87,631,425	8,763
Issued during the year	–	–	1,645	–
At 31st December 2004	96,000,000	9,600	87,633,070	8,763

The shares issued during the year were issued for cash consideration of £2,000 to employees exercising share options under share option schemes.

Notes to the Financial Statements
for the year ended 31st December 2004

24 Share premium account and reserves

	Share premium account £000	Other reserves £000	Profit and loss account £000
Group			
At 1st January 2004	43,222	864	36,140
Issue of shares	2	–	–
Loss for the year	–	–	(58,190)
Dividends	–	–	(1,314)
At 31st December 2004	43,224	864	(23,364)

At 31st December 2004, goodwill written off directly against profit and loss reserves in respect of subsidiaries still held by the Group was £16,891,000 (31st December 2003 – £16,891,000).

	Share premium account £000	Other reserves £000	Profit and loss account £000
Company			
At 1st January 2004	43,222	25,750	282,977
Issue of shares	2	–	–
Loss for the year	–	–	(209,777)
Dividends	–	–	(1,314)
At 31st December 2004	43,224	25,750	71,886

Included in other reserves are £21,512,000 of distributable reserves relating to foreign exchange and acquisition reserves and £4,238,000 of non-distributable reserves. The profit and loss reserves of the Company include £49,307,000 that is not distributable.

The Company's loss for the year reflects the impact of certain transactions with other Group companies that formed part of an internal reorganisation of the Group structure.

25 Notes to the cash flow statement

	2004 £000	2003 £000
Reconciliation of operating profit to net cash inflow from operations		
Operating profit	**11,802**	20,392
Amortisation and impairment of goodwill	**8,841**	8,398
Depreciation	**4,636**	5,418
Net (profit)/loss on sale of tangible fixed assets	**(128)**	331
Decrease in provisions	**(989)**	(1,646)
Decrease in debtors	**7,778**	2,607
Decrease in creditors	**(2,326)**	(10,510)
Net cash inflow from operating activities	**29,614**	24,990

	2004 £000	2003 £000
Reconciliation of net cash flow to movement in net debt		
Decrease in cash and increase in overdraft	**(2,699)**	(4,354)
Decrease in finance leases	**14**	479
Decrease/(Increase) in loans	**7,407**	(25,708)
	4,722	(29,583)
Net debt at 1st January 2004	**(89,344)**	(59,761)
Net debt at 31st December 2004	**(84,622)**	(89,344)

25 Notes to the cash flow statement continued

	Loans and finance leases repayable in less than one year £000	Loans and finance leases repayable in more than one year £000	Overdraft £000	Cash £000	Total £000
Analysis of movements in loans and cash balances					
At 1st January 2004	(1,421)	(90,000)	(851)	2,928	(89,344)
Decrease/(increase) in loans and net cash inflow	1,421	6,000	(750)	(1,949)	4,722
At 31st December 2004	–	(84,000)	(1,601)	979	(84,622)

26 Operating lease commitments

The Group has numerous premises operated under leases whose terms, conditions and expiry dates vary considerably, some of which are no longer occupied by the Group. In addition, the Group leases items of plant and equipment and in particular has entered into a contract hire agreement to lease motor vehicles.

The net commitment in respect of operating leases in 2005 is as follows:

	Plant and equipment including motor vehicles £000	Land & buildings occupied by Group £000	Land & buildings not occupied by Group £000	Total £000
For leases expiring				
within one year	446	145	420	1,011
between two and five years	216	353	–	569
beyond five years	–	310	1,153	1,463
	662	808	1,573	3,043

27 Pension commitments

The Group has continued to account for pensions in accordance with SSAP 24 and the disclosures given in (a) are those required by that standard. FRS 17 Retirement Benefits was issued in November 2000 but will not be mandatory for the Group and Company until the year ending 31st December 2005. Prior to this, phased transitional disclosures are required.

a) Group pension schemes

The Group operates two funded pension schemes providing benefits based on final pensionable salary. The two schemes are the Nestor Healthcare Group Retirement Benefits Scheme (the Nestor Scheme) and the Healthcall Group Limited Pension Scheme (the Healthcall Scheme). Both schemes are closed to new members. The schemes are administered by Trustees separately from the affairs of the Group and are contracted out of the additional component of the State Pension Scheme.

Nestor Scheme

Watson Wyatt LLP, consulting actuaries, carried out an actuarial valuation of the Nestor Scheme as at 5th April 2003. On the actuarial basis used, as at that date, the assessed value of the assets was 62% of the value placed on the liabilities in respect of benefits earned to 5th April 2003, allowing for expected future increases in pensionable earnings to Normal Pension Age, treating the scheme as an ongoing entity.

The market value of the investments held in the Nestor Scheme as at the valuation date was £9,923,000. In addition there were pensions in payment secured by the purchase of annuities.

The assumptions which have the most significant effect on the results of the valuation are those relating to the rate of investment return on future net cash flow and the rate of increase in pensionable earnings. These rates were set relative to an assumed long-term rate of price inflation of 2.5% per annum.

The assumed future rate of investment return, used to discount projected income and outgoing benefits, was a real rate of 2.0% per annum relative to price inflation for pensioners and 5.0% per annum before retirement and 3.0% per annum after retirement for non-pensioners. Pensionable earnings were assumed to increase on average at a rate of 2.0% per annum ahead of price inflation with promotional increases assumed in addition.

27 Pension commitments continued

Nestor Scheme continued

The employer's contribution rate, currently 22.4% (32.4% for certain current and past executive directors), is calculated using the projected unit method and the shortfall of assets as at 5th April 2003 is amortised as a constant percentage of members' pensionable earnings over the average expected working lifetime of the active members. As the Nestor Scheme is closed to new members, under the projected unit method the employer's contribution rate will increase as the members of that scheme approach retirement.

Healthcall Scheme

Watson Wyatt LLP, consulting actuaries, carried out an actuarial valuation of the Healthcall Scheme as at 1st November 2001. On the actuarial basis used, as at that date, the assessed value of the assets was 51% of the capitalised value of the accrued benefits, allowing for expected future increases in pensionable earnings to Normal Pension Age, treating the scheme as an ongoing entity.

The market value of the investments held in the scheme as at the valuation date was £5,346,000. In addition there were pensions in payment secured by the purchase of annuities.

The assumptions which have the most significant effect on the results of the valuation are those relating to the rate of investment return and the rate of increase in pensionable earnings. These rates were set relative to an assumed long-term rate of price inflation of 2.3% per annum.

The assumed future rate of investment return, used to discount projected income and outgoing benefits, was a real rate of 3.0% per annum relative to price inflation for pensioners and 4.0% per annum before retirement and 3.0% per annum after retirement for non-pensioners. Pensionable earnings were assumed to increase on average at a rate of 2.0% per annum ahead of price inflation.

The employer's contribution rate, currently 21.0%, is calculated using the projected unit method and the shortfall of assets as at 1st November 2001 is amortised as annual payments of £500,000 over the average remaining expected service lives of the active members. As the Healthcall scheme is closed to new members, under the projected unit method, the employer's contribution rate will increase as the members of that scheme approach retirement.

Other schemes

The Group also operates several defined contribution schemes with varying rates of employer contribution.

Pension charge

The pension charge for the year was £2,187,000 (2003: £2,364,000). At 31st December 2004 £121,000 of this amount had yet to be paid to the respective schemes (2003: £143,000).

At 31st December 2004, there was a net pension liability of £4,158,000 (2003: £4,436,000) included within provisions. This relates to the formal valuation of the Healthcall Scheme as at the date of acquisition, adjusted for subsequent movements. This liability is expected to be satisfied by the annual payments of £500,000 up to 2015 as referred to above.

b) FRS 17 Retirement Benefits

The valuation used for FRS 17 disclosures has been based on the results of an actuarial valuation of the Nestor Scheme as at 5th April 2003 and on the last formal actuarial valuation of the Healthcall Scheme as at 1st November 2001 and updated by Watson Wyatt LLP to take account of the requirements of FRS 17 in order to assess the liabilities of the schemes at 31st December 2004. Assets of the schemes are stated at their market valuation at 31st December 2004.

The financial assumptions used to calculate the schemes' liabilities under FRS 17 are:

	At 31st December 2004	At 31st December 2003	At 31st December 2002
Valuation method	**Projected unit**	Projected unit	Projected unit
Discount rate	**5.40%**	5.50%	5.75%
Inflation rate	**2.80%**	2.75%	2.25%
Increases to pensions in payment and deferred pensions*	**2.80%**	2.75%	2.25%
Salary increases	**4.80%**	4.75%	4.25%

* Different increases assumed for certain elements of pension

27 Pension commitments continued

The assets in the schemes and the expected rates of return were:

	Long-term rate of return expected on 31st December 2004	**Value at 31st December 2004 £000**	Long-term rate of return expected on 31st December 2003	Value at 31st December 2003 £000	Long-term rate of return expected on 31st December 2002	Value at 31st December 2002 £000
Equities	**8.0%**	**19,362**	8.0%	17,171	8.0%	11,590
Bonds	**4.8%**	**1,968**	5.0%	1,993	5.0%	2,276
Other	**4.0%**	**2,207**	4.0%	604	4.0%	896
Total market value of assets		**23,537**		19,768		14,762
Present value of schemes' liabilities		**(38,752)**		(35,439)		(27,535)
Deficit in the schemes – pension liabilities		**(15,215)**		(15,671)		(12,773)
Related deferred tax asset		**4,565**		4,701		3,832
Net pension liability		**(10,650)**		(10,970)		(8,941)

The movement in the deficit in the schemes during the year was:

	31st December 2004 £000	31st December 2003 £000
Deficit in the schemes at beginning of year	**(15,671)**	(12,773)
Contributions paid	**2,388**	2,355
Current service cost	**(1,500)**	(1,635)
Other finance charge	**(412)**	(465)
Actuarial loss	**(20)**	(3,153)
Deficit in the schemes at end of year	**(15,215)**	(15,671)

As stated on page 50, a provision has been made for the deficit on the Healthcall scheme as of the date of acquisition. Therefore, the net effect on the Group's net assets and profit and loss reserves of the deficit in the schemes' assets would be:

	2004 Group £000	2003 Group £000
Net assets		
Net assets	**29,537**	88,921
Add: existing accrued pension liability	**4,158**	4,436
Deferred tax on existing accrued pension liability	**(1,247)**	(1,331)
Less: total pension liabilities	**(15,215)**	(15,671)
Deferred tax on total pension liabilities	**4,565**	4,701
Net assets including pension liabilities	**21,798**	81,056

	2004 Group £000	2003 Group £000
Reserves		
Profit and loss reserve	(23,364)	36,140
Add: existing accrued pension liability	4,158	4,436
Deferred tax on existing accrued pension liability	(1,247)	(1,331)
Less: total pension liabilities	(15,215)	(15,671)
Deferred tax on total pension liabilities	4,565	4,701
Profit and loss reserve including pension liabilities	(31,103)	28,275

Notes to the Financial Statements

for the year ended 31st December 2004

27 Pension commitments continued

Components of defined benefit cost for the year ended 31st December 2004

Analysis of amounts that would be charged to operating profit	**2004 Group £000**	2003 Group £000
Current service cost	**1,500**	1,635

Analysis of amounts that would be charged to other finance income		
Interest on pension scheme liabilities	**1,969**	1,619
Expected return on assets in the pension scheme	**(1,557)**	(1,154)
Net charge to other finance income	**412**	465
Total profit and loss charge before deduction for tax	**1,912**	2,100

Analysis of amounts that would be recognised in statement of total recognised gains and losses	**2004 Group £000**	2003 Group £000
Actual return less expected return on scheme assets	**554**	1,834
Experience gains/(losses) arising on the scheme liabilities	**483**	(112)
Changes in the assumptions underlying the present value of the scheme liabilities	**(1,057)**	(4,875)
Actuarial loss recognised in statement of total recognised gains and losses	**(20)**	(3,153)

History of experience gains and losses	**2004 Group**	2003 Group	2002 Group
Difference between the actual and expected return of scheme assets:			
Amount (£000)	**554**	1,834	(4,691)
Percentage of scheme assets	**2.4%**	9.3%	(31.8%)
Experience gains and (losses) on scheme liabilities:			
Amount (£000)	**483**	(112)	(440)
Percentage of present value of scheme liabilities	**1.2%**	(0.3%)	(1.6%)
Total amount recognised in statement of total recognised gains and losses:			
Amount (£000)	**(20)**	(3,153)	(7,162)
Percentage of present value of scheme liabilities	**(0.1%)**	(8.9%)	(26.0%)

28 Share option schemes

The following table sets out options in issue under the various Company schemes at the beginning and end of the year and movements during the year. Share options in issue expire after a certain time and exercise dates vary. Exercise rights are subject to the rules of the schemes and share options in issue are not normally exercisable until the expiry of a period of at least three years. In addition, achievement of performance targets is normally required in all schemes except the SAYE scheme.

The Group has taken advantage of the exemption applicable to Inland Revenue Approved SAYE share option schemes under UITF Abstract 17 (revised 2003), "Employee Share Schemes".

	Date of issue	Option price (pence)	In issue 1st Jan 2004	Granted in the year	Exercised in the year	Lapsed in the year	In issue 31st Dec 2004
Company Share Option Plan 1996							
	April 1998	236.50	4,661	–	–	–	4,661
	October 1998	339.50	4,602	–	–	–	4,602
	April 1999	407.50	21,712	–	–	(4,171)	17,541
	October 1999	596.50	26,875	–	–	–	26,875
	May 2000	425.00	213,750	–	–	(54,454)	159,296
	August 2000	429.50	6,984	–	–	–	6,984
	November 2000	472.50	6,349	–	–	–	6,349
	March 2001	542.50	51,627	–	–	(17,903)	33,724
	October 2001	510.00	47,056	–	–	(11,764)	35,292
	April 2002	544.00	11,028	–	–	–	11,028
			394,644	–	–	(88,292)	306,352
Employee Share Option Scheme 1996							
	April 1998	236.50	63,687	–	–	–	63,687
	April 1999	407.50	47,558	–	–	(15,955)	31,603
	October 1999	596.50	2,850	–	–	–	2,850
	May 2000	425.00	348,894	–	–	(81,588)	267,306
	August 2000	429.50	6,985	–	–	–	6,985
	November 2000	472.50	46,561	–	–	–	46,561
	March 2001	542.50	209,230	–	–	(50,082)	159,148
	October 2001	510.00	89,433	–	–	(18,551)	70,882
	April 2002	544.00	39,522	–	–	–	39,522
			854,720	–	–	(166,176)	688,544
Share Option Plan 2002							
	July 2002	267.50	730,133	–	–	(162,919)	567,214
	October 2002	212.50	322,352	–	–	–	322,352
	June 2003	273.50	112,248	–	–	–	112,248
	November 2003	301.00	304,500	–	–	(59,000)	245,500
			1,469,233	–	–	(221,919)	1,247,314
Savings Related Share Option Scheme							
	December 1998	305.00	15,927	–	–	(15,927)	–
	September 1999	412.00	6,875	–	–	(1,310)	5,565
	April 2001	447.20	44,491	–	–	(30,388)	14,103
	April 2002	454.80	99,687	–	–	(56,216)	43,471
	April 2003	157.12	818,187	–	(1,645)	(354,100)	462,442
	April 2004	156.96	–	374,606	–	(108,437)	266,169
			985,167	374,606	(1,645)	(566,378)	791,750
Total			**3,703,764**	**374,606**	**(1,645)**	**(1,042,765)**	**3,033,960**

Five Year Summary

	2000 £000	2001 £000	2002* £000	2003 £000	**2004** **£000**
Group profit and loss account					
Turnover from continuing operations	292,802	400,965	482,695	423,161	**389,839**
Turnover	292,802	400,965	482,695	423,161	**389,839**
Operating profit from continuing operations	17,124	21,629	29,669	20,392	**11,802**
Operating profit	17,124	21,629	29,669	20,392	**11,802**
Exceptional items	(727)	(4,574)	(17,300)	(2,680)	**(62,021)**
(Loss)/profit on ordinary activities before interest	16,397	17,055	12,369	17,712	**(50,219)**
Net interest	425	(1,544)	(4,238)	(4,110)	**(5,418)**
(Loss)/profit before taxation	16,822	15,511	8,131	13,602	**(55,637)**
Taxation	(5,190)	(6,013)	(6,052)	(4,353)	**(2,435)**
(Loss)/profit after taxation	11,632	9,498	2,079	9,249	**(58,072)**
Equity minority interests	(158)	(19)	(48)	(47)	**(118)**
(Loss)/profit attributable to shareholders	11,474	9,479	2,031	9,202	**(58,190)**
Profit before taxation, goodwill amortisation and exceptional items	18,759	23,916	33,062	24,680	**15,225**
Basic (loss)/earnings per share – FRS 3 basis	14.63p	11.55p	2.33p	10.51p	**(66.40p)**
Basic earnings per share – before goodwill amortisation and exceptional items	17.10p	20.54p	29.90p	23.17p	**11.98p**
Dividends per share	6.69p	8.02p	9.62p	9.62p	**1.50p**

* 2002 has been restated to reflect the full adoption of FRS 19. 2000-2001 have not been restated as it is not practicable to determine the impact of FRS 19 with sufficient accuracy.

	2000 £000	2001 £000	2002* £000	2003 £000	**2004 £000**
Group balance sheet					
Goodwill	31,428	152,507	138,049	161,085	**106,767**
Tangible fixed assets	7,776	13,512	12,741	12,968	**7,534**
Investments	28	28	1	–	**–**
Total fixed assets	39,232	166,047	150,791	174,053	**114,301**
Current assets	40,926	66,024	59,187	61,496	**54,072**
Liabilities and provisions	(36,247)	(63,131)	(61,898)	(57,284)	**(54,214)**
Net operating assets	43,911	168,940	148,080	178,265	**114,159**
Net cash/(borrowings)	8,929	(75,350)	(59,761)	(89,344)	**(84,622)**
Net assets	52,840	93,590	88,319	88,921	**29,537**
Share capital	7,853	8,708	8,747	8,763	**8,763**
Share premium account	4,868	42,298	43,022	43,222	**43,224**
Other reserves	39,788	42,271	36,229	37,004	**(22,500)**
Equity shareholders' funds	52,509	93,277	87,998	88,989	**29,487**
Equity minority interests	331	313	321	(68)	**50**
	52,840	93,590	88,319	88,921	**29,537**
Group cash flow statement					
Net cash inflow from operating activities before exceptional items	23,760	24,648	54,144	24,990	**29,614**
Cash flow from exceptional items	–	(2,246)	(2,300)	(1,899)	**(2,922)**
Interest (paid)/received	510	(964)	(3,896)	(3,744)	**(5,556)**
Tax paid	(3,776)	(6,268)	(6,240)	(5,711)	**(3,930)**
Capital expenditure	(2,365)	(4,523)	(6,743)	(5,730)	**(2,543)**
Acquisitions and disposals	(11,867)	(124,934)	(12,640)	(29,285)	**(4,562)**
Equity dividends paid	(4,674)	(5,883)	(7,499)	(8,420)	**(5,381)**
Issue of shares	275	38,285	763	216	**2**
Increase/(decrease) in loans	(60)	69,679	(10,404)	25,229	**(7,421)**
Increase/(decrease) in cash	1,803	(12,206)	5,185	(4,354)	**(2,699)**

* 2002 has been restated to reflect the full adoption of FRS 19. 2000-2001 have not been restated as it is not practicable to determine the impact of FRS 19 with sufficient accuracy.

Shareholder Information

Financial calendar

Announcement of 2005 results (provisional)

For the half-year	August 2005
For the year	March 2006
Annual Report and Accounts circulated	March 2006
Annual General Meeting	April 2006

Dividends

Proposed final dividend 2004	
Announcement	7th March 2005
Ex-dividend	4th May 2005
Record date	6th May 2005
Payment date	3rd June 2005
Interim dividend 2005 (provisional)	
Announcement	August 2005
Payment	October 2005

Analysis of shareholdings

At the date of this report the Company has 1,449 shareholders who hold 87,633,070 ordinary shares between them, analysed as follows:

Size of holding	Number of shareholders	% of shareholders	Number of shares	% of shares
1 – 5,000	1,147	79	1,257,047	1
5,001 – 50,000	194	13	3,046,287	4
50,001 – 100,000	30	2	2,120,833	2
100,001 and over	78	6	81,208,903	93
	1,449	100	87,633,070	100

Type of shareholder				
Individuals	962	66	2,192,988	3
Nominee companies*	443	31	85,126,722	97
Other corporate and public bodies	40	3	303,639	–
Trust companies	4	–	9,721	–
	1,449	100	87,633,070	100

* This category includes the beneficiaries of pension funds, unit trusts, life assurance companies and investment trusts.

Share Registrar

The Company's registrar is Computershare Investor Services PLC, PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH.

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